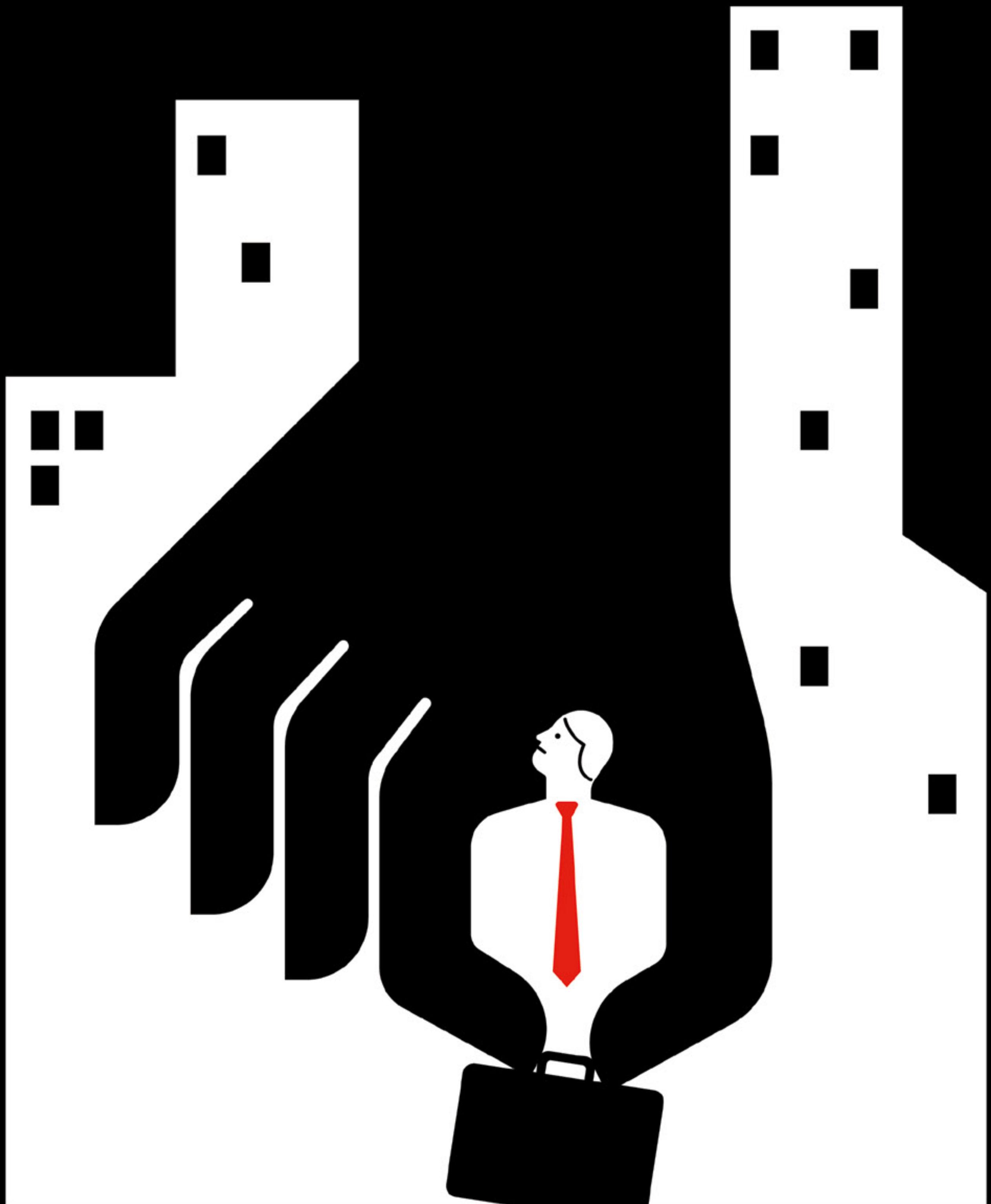
HISCOX

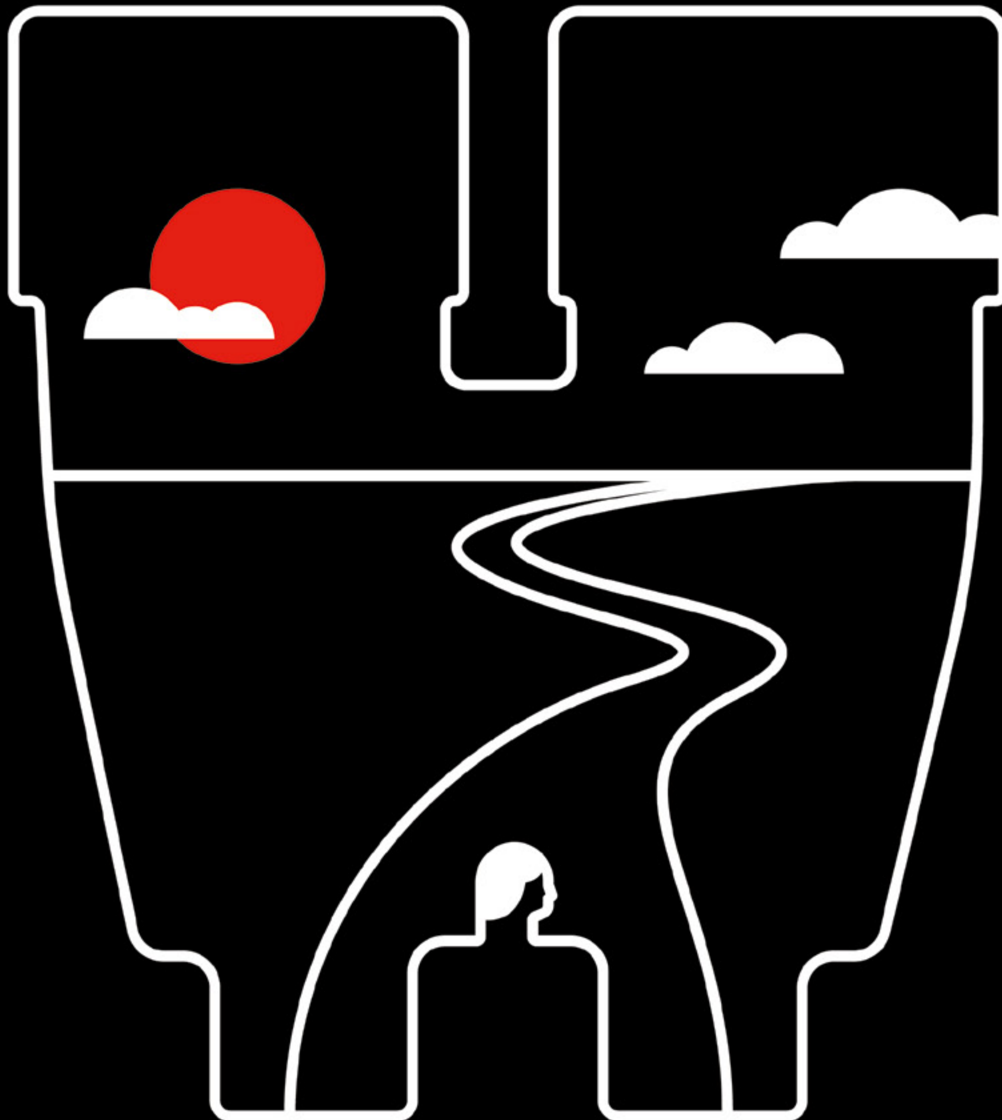
Hiscox Ltd
Report and Accounts
2018



Hiscox is a diversified international insurance group with a powerful brand, strong balance sheet and plenty of room to grow. We are listed on the London Stock Exchange, headquartered in Bermuda and currently have over 3,300 staff across 14 countries and 34 offices. We can trace our roots back to 1901 and have grown organically over time from our beginnings in the Lloyd's market.

Our ambition is to be a respected specialist insurer in key geographies and product lines, valued by our customers, business partners and shareholders. Our values define our business, with a focus on quality, courage, excellence in execution and our people.

A specialist approach
See page 29.



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Strategic report

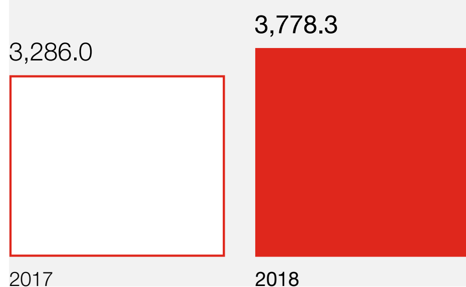
Financial highlights

$3,778.3m
Gross premiums written increased by 15%.

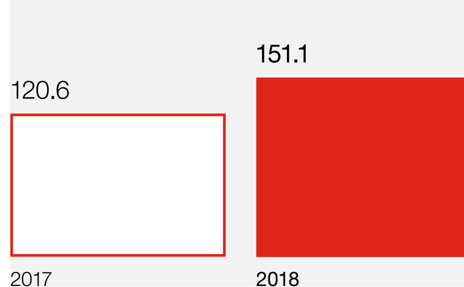
$151.1m
Profit before tax excluding foreign exchange up by 25%.

41.9¢
Total ordinary dividend per share up by 5.2%.

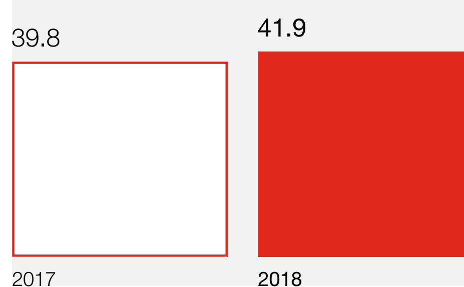
Gross premiums written ($m)



Profit before tax excluding FX ($m)



Ordinary dividend (¢ per share)



Group key performance indicators*

	2018	2017
Gross premiums written ($m)	3,778.3	3,286.0
Net premiums earned ($m)	2,573.6	2,416.2
Profit before tax ($m)	137.4	39.7
Profit before tax excluding foreign exchange ($m)	151.1	120.6
Profit after tax ($m)	128.0	33.9
Earnings per share (¢)	45.1	12.0
Total ordinary dividend per share for year (¢)	41.9	39.8
Net asset value per share (¢)	819.1	835.1
Combined ratio (%)	94.9	99.9
Combined ratio excluding foreign exchange (%)	94.4	98.8
Return on equity (%)	5.6	1.5
Investment return (%)	0.7	2.0
Reserve releases ($m)	326.5	324.2

*Additional performance measures are discussed on page 28.

Why invest in Hiscox?

Hiscox is a diversified international insurance group with a consistent, long-held strategy that provides opportunities throughout the insurance cycle. We are a uniquely-balanced insurer with a powerful brand, strong balance sheet and plenty of room to grow.

Our strategy

Our success is due to our long-held strategy:
- to use our underwriting expertise in Bermuda and London to write larger premium, volatile or complex risks;
- to build distribution in the UK, Europe, USA and Asia for our specialist retail products;
- to protect and nurture our distinctive culture by recruiting the best people, and by focusing on organic growth.

This strategy provides opportunities throughout the insurance cycle, allowing us to deliver in the short, medium and long term.

Long-term shareholder value

Hiscox has always had a focus on creating long-term shareholder value with a progressive dividend policy.

Over the last five years ROE averaged 13%, above the FTSE All-Share average of 11%. This performance has enabled the Company to distribute $1,123 million to shareholders since 2014, and deliver a total shareholder return of 67% – well above the FTSE All-Share of 20%.

Building balance – a symbiotic relationship

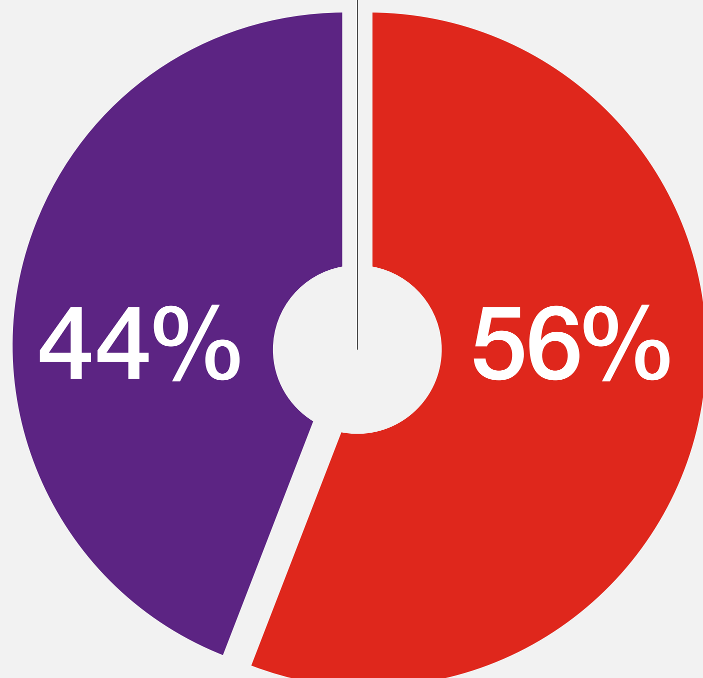
Total Group controlled income for 2018 (%)

Big-ticket business

- Larger premium, globally traded, catastrophe-exposed business written mainly through Hiscox London Market and Hiscox Re & ILS.
- Shrinks and expands according to pricing environment.
- Excess profits allow further investment in retail development.

Retail business

- Smaller premium, locally traded, relatively less volatile business written mainly through Hiscox Retail.
- Growth between 5-15% per annum.
- Pays dividends.
- Specialist knowledge differentiates us and investment in brand builds strong market position.
- Profits act as additional capital.



The Hiscox Group employs more than 3,300 people across 14 countries and 34 offices. Our products and services reach every continent and we are not overly reliant on any one of our divisions for the Group's overall profits.

Operational highlights

Hiscox Retail
The single biggest segment in the Group wrote over $2 billion of income, served one million customers, and its profits cover the dividend for the third year in a row.

Brexit
Our business is ready for Brexit; our new European subsidiary Hiscox SA is fully operational and we are already utilising the Lloyd's Brussels subsidiary.

Hiscox London Market
Returned to good health after several years of taking tough action, and successfully replaced $400 million of challenged business with more attractive risks by the end of 2018.

Claims
We paid out £1.2 billion in claims in 2018 – getting our customers back on their feet when the worst happened.

Hiscox Re & ILS
Demand for our ILS offering has been sustained, with assets under management now exceeding $1.5bn after last year's losses.

$1.5bn

Marketing
Our commitment to building a differentiated brand continued in 2018, with award-winning campaigns such as CyberLive in the UK driving double-digit premium growth in our small business offering.

A track record of profitable growth

Over the last five years the Hiscox Group has:

increased gross premiums written by 31% to

$3.78bn

achieved compound dividend growth in constant currency of

9.9%

returned capital to shareholders of

$1,123m

delivered an average combined ratio of

89.6%

reported average return on equity of

12.6%

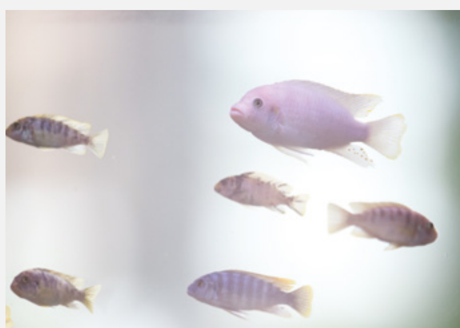
We have invested significantly in creating a unique culture that reflects our values and customer-focused ethos, and a powerful, differentiated brand which our target clients can identify with.

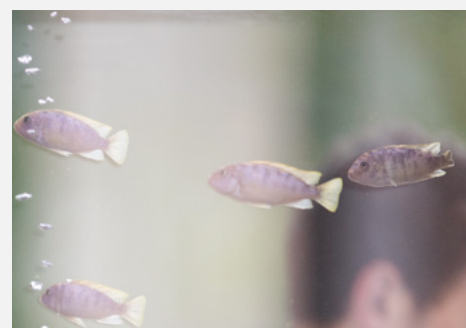
A unique culture

The excellence of our people has been a crucial factor in our continuing success. Their expertise, courage and dedication continue to drive our reputation for quality and professionalism. In return, we strive to provide them with a work environment in which they can flourish.

In our annual global employee engagement survey we looked at how connected employees feel to Hiscox, their managers, teams and roles. Hiscox enjoys very high employee engagement, which averages in the top quartile of over 200 companies worldwide. In 2018, 86% of our employees said they are proud to work for us, 94% said they believe in our corporate values and 80% said they would recommend Hiscox as a great place to work.

Pleasingly, Hiscox also ranked seventh in Glassdoor's annual Employees' Choice Awards for the UK's Best Places to Work, up from eighth place last year. This accolade is especially important to us as the listing is based on the feedback that employees have shared about us on Glassdoor over the past year.





We have specialist knowledge and great relationships, and we care about our customers and each other. We have always believed that doing the right thing, however hard, will lead to success. In 2018 this approach resulted in us receiving a number of new accolades.

Awards

Hiscox Group

- Hiscox ranked seventh in Glassdoor's annual Employees' Choice Awards for the UK's Best Places to Work – up from eighth place last year.
- Hiscox received Insurance Company of the Year 2018 at UK newspaper City A.M.'s annual awards.
- Bronek Masojada received Outstanding Contributor of the Year – Risk at the Insurance Insider Honours Awards 2018.

Big-ticket business

- Hiscox Security Incident Response product won the Innovation Award at Business Insurance magazine's Innovation Awards 2018.
- Hiscox London Market received Underwriting Team of the Year for our FloodPlus product, and Rising Star of the Year for product recall and terrorism underwriter Amie Townsend at the Insurance Day London Market Awards 2018.

Retail business

- Hiscox USA picked up six awards at the Financial Communications Society's 24th Annual Portfolio Awards for its 'I'mpossible' and 'Has America Lost its Courage?' advertising campaigns.
- Hiscox UK was recognised with a Marketing New Thinking Award for its CyberLive advertising campaign, thanks to its use of data creativity in brand-building, and a Media Week Award in the Media Idea (Budget Under £250,000) category.

Our values guide our business: to have courage and integrity, to provide quality products, to excel in the service we provide and, above all, to be human. At the heart of our business is a restless spirit to challenge convention in our industry, and in ourselves, to always do better.

As we grow, we've always got one eye on making sure our values remain front and centre. In 2019 our Chief Executive is leading a project to refresh them once again.

Values

Chairman's statement

Hiscox delivered a good profit before tax of $137.4 million (2017: $39.7 million) despite another busy year for claims. After a relatively benign start, we saw a number of natural catastrophes and significant market losses in the second half which, combined with turbulent financial markets, have impacted our result.

$137.4m

Hiscox delivered a good profit before tax of $137.4 million (2017: $39.7 million) despite another busy year for claims.

Our long-held strategy of balancing the volatility of big-ticket lines with more steady retail earnings continues to serve us well, and the strength of our products, people and brand mean we are able to seize opportunities.

Our retail businesses had a good year, delivering double-digit growth and solid profits as we reached the milestone of one million retail customers. Our business in the USA continues to develop strongly, however as we continue to exercise discipline in the under-performing directors and officers' account, growth will be tempered.

In big-ticket lines, market conditions have been challenging but our London Market business has reaped the rewards of the tough action we have taken over the last three years to reduce or exit from unprofitable lines, and returned to excellent growth and profitability.

Our reinsurance and ILS operations experienced a very active year for claims, with exposure to hurricanes and wildfires in the US, typhoons in Japan, hailstorms in Australia and large claims in cyber and marine hull.

In our investments, we were impacted by both difficult equity markets and the value of our bond portfolio which naturally reduced as interest rates rose in the US. We will benefit from those same rising interest rates in 2019 and recover 2018 losses as we hold the bonds to maturity.

Financial performance

The result for the year ending 31 December 2018 was a profit before tax excluding foreign exchange of $151.1 million (2017: $120.6 million). Gross premiums written increased by 15.0% to $3,778.3 million (2017: $3,286.0 million). The combined ratio was 94.9% (2017: 99.9%). Earnings per share increased to 45.1¢ (2017: 12.0¢) and the net asset value per share decreased to 819.1¢ (2017: 835.1¢). Post-tax return on equity was 5.6% (2017: 1.5%). Our investment return of $42.5 million (2017: $112.5 million), before derivatives and fees, equates to a return of 0.7% (2017: 2.0%) on total assets under management.

I am pleased to announce a final dividend of 28.6¢, which is an increase of 5.2%. The record date for the dividend will be 10 May 2019 and the payment date will be 12 June 2019.

The Board has approved a scrip alternative subject to the terms and conditions of Hiscox Ltd's 2016 Scrip Dividend Scheme. The last date for receipt of scrip elections will be 20 May 2019 and the reference price will be announced on 30 May 2019.

Our market

We are ruled by the market, particularly in big-ticket and reinsurance lines, and adjust our appetite according to the

opportunities it provides. Rates did not respond as much as we feel they should have following the losses arising from hurricanes Harvey, Irma and Maria in 2017, but where they did we were able to take advantage. A second successive year of historic market losses seems to have done little to spur a widespread market turn, but once again we have been ready, taking opportunities where they have been available.

In London, the Lloyd's Decile 10 work is making good progress to redress the balance when it comes to capacity and market discipline. We have been very supportive of Lloyd's, which has put pressure on the market's underwriters to take action in unprofitable areas. I feel it strange that it takes a regulator to tell businesses that it is a bad thing to lose money, but the process has certainly squeezed out some of the worst performing lines and that is a very good thing indeed.

Although the reinsurance market did not harden as many had hoped, the retrocession market – reinsurance of reinsurers – did become more sensibly priced. This has in the past led to sufficient increases all the way through to insurance pricing. It remains to be seen whether that particular tail still wags the dog.

Progress can feel painstaking, but we are gaining ground on improved rates, and on the technical, but important, area of terms and conditions. As our London Market result shows, we are happy to navigate these waters and our underwriters are up to the task.

People and culture

People and culture make a difference; indeed, culture and values are as important as strategy and distribution, so when it comes to values we expect our top executives and the Board to show leadership. As Hiscox continues to grow, the continuity of our culture is key. It has been pleasing this year to see strong succession from within and, in retail, the top team sharing their expertise with different parts of our business to help drive Hiscox to the next level.

I am regularly told by those that know us that Hiscox has a distinctive culture underpinned by strong values. Being the highest ranking financial services firm in Glassdoor's 2019 best places to work in the UK, and receiving very positive customer feedback, validates that our values are being lived. We do not take this for granted, and around every five years, as new people join and the business evolves, we undertake an exercise to refresh them. I am pleased that we are embarking upon another such exercise, led by our Chief Executive Bronek. It doesn't mean that we feel they are wrong – language becomes dated and core principles need to be expressed so they resonate with new generations of employees. Our values inform all our day-to-day decisions and that makes them critical to maintaining our reputation for integrity and decent and fair behaviour in everything we do.

> In the London Market, it has been a war of attrition but rates and terms are improving in many lines and the refinements we have already made to the portfolio mean we are well positioned as renewed discipline courses through the market.
>
> Outlook

Outlook

The diversity of our products and distribution continues to give us options. Our retail operations have again balanced the volatility of the big-ticket lines, validating our long-held strategy. We have talked before about the moderating percentage growth rate in Hiscox USA, but we find the size of the US opportunity exciting.

In the London Market, it has been a war of attrition but rates and terms are improving in many lines and the refinements we have already made to the portfolio mean we are well positioned as renewed discipline courses through the market. Similarly in reinsurance, we believe opportunities will present themselves in loss-affected accounts. We also expect to benefit from improved investment conditions.

2018 was a year of change and achievement in our operations, and more change is planned in 2019. Although we have completed our structural readiness for Brexit, our investment in infrastructure projects that will boost our abilities to serve customers and create efficiencies continues. This is all good, necessary work, but as we have mentioned previously it will have an impact on growth and expenses in the short term.

I would like to finish by thanking everyone at Hiscox for their efforts this year, particularly as we entered the FTSE 100. Their hard work in serving our customers, paying claims, establishing new partnerships, building new systems and supporting our growth has all contributed to this result.

Robert Childs
25 February 2019

Chief Executive's report

2018 was another eventful year for insurers, with catastrophe activity at historic levels, financial market turmoil and geopolitical uncertainty. In this challenging environment, Hiscox grew gross premiums written by 15.0% to $3,778.3 million and more than tripled profits to $137.4 million (2017: $39.7 million). Our post-tax return on equity was 5.6%, an improvement on last year's 1.5%, and a fair result in the circumstances.

$3,778.3m

Hiscox has grown gross premiums written by 15.0% to $3,778.3 million and more than tripled profits to $137.4 million.

The standout performer in 2018 was Hiscox London Market, which returned to growth and profit after three years of tough action; withdrawing from poor-performing lines and navigating challenging markets. Having done much of the hard work, the team was in a good position to navigate the Lloyd's Decile 10 profit remediation programme.

Hiscox Retail wrote over $2 billion of premium, served one million customers and has become a strong profit generator for the Group, with its profits covering the dividend for the third consecutive year. As a result of portfolio optimisation, we expect growth in Hiscox Retail to be in the high single digits for the next 12 months.

Hiscox Re & ILS has been hit by a second year of catastrophe claims. Our aggregate protection products, our risk excess covers and some specialty areas – all areas of focus since 2012 – meant that the higher frequency of mid-sized catastrophes and individual large losses in 2018 hit us harder than 2017's fewer but larger catastrophes. Our products worked, our clients are happy, and while it cost us more, that is the nature of our business.

Our ambition for 2019 is to continue to grow premiums, albeit at a slightly slower pace than 2018. We are hopeful that positive pricing momentum and ongoing portfolio optimisation will lead to improved underwriting profits, with higher interest rates driving better investment returns.

I review each part of our business in turn below.

Hiscox Retail

Generating profits and creating value; investment in brand and infrastructure continues

Hiscox Retail comprises Hiscox UK & Europe and Hiscox International. In this division, our specialist knowledge and retail products differentiate us and our ongoing investment in brand helps us build a strong market position. Hiscox Retail is the single biggest segment in the Group and this year generated 55% of the Group's gross premiums written at $2,087.1 million (2017: $1,835.4 million), up 13.7% year-on-year. Our ambition remains to grow our retail business between 5% and 15% per annum in the medium term. We reached the milestone of one million retail customers and $2 billion of premiums during the year, and the fact that our market shares remain small in most of our markets indicates the size of the opportunity still ahead of us. Building a retail business takes time, but persistence pays off. We continue to invest in building our brand across all markets and in multi-year IT infrastructure programmes that will support our growth plans.

Hiscox Retail delivered profits of $136.0 million (2017: $141.6 million),

We reached the milestone of one million retail customers and $2 billion of premiums during the year, and the fact that our market shares remain small in most of our markets indicates the size of the opportunity still ahead of us.

Hiscox Retail

Hiscox Retail

	2018 $m	2017 $m
Gross premiums written	2,087.1	1,835.4
Net premiums earned	1,821.9	1,585.3
Underwriting profit	125.4	114.7
Investment result	9.5	29.4
Foreign exchange and other*	1.1	(2.5)
Profit before tax	136.0	141.6
Combined ratio	93.6	94.6
Combined ratio excluding foreign exchange	93.6	94.5

*Includes impairments and accelerated amortisation.

and the combined ratio of 93.6% (2017: 94.6%) is within our 90%-95% target range. The improvement in combined ratio on the larger premium base was insufficient to offset lower investment returns, leading to lower profits from the division. The rating environment across retail also remained broadly flat throughout 2018.

We made some important leadership changes across retail in 2018. As previously announced, Ben Walter moved from CEO of Hiscox USA to the newly created role of CEO Hiscox Global Retail. Ben is helping to sharpen the focus of our retail operations, and address the common challenges that our retail businesses face when it comes to driving product innovation, creating scale and digitising for the modern age. In addition, Steve Langan moved from CEO of Hiscox UK & Ireland to CEO of Hiscox USA while remaining Chief Marketing Officer for the Group. Steve has the business-building experience and branding firepower that our US operations require for their next phase of growth. Bob Thaker, who is currently serving as CEO of DirectAsia, will succeed Steve as Hiscox UK CEO in the first quarter of 2019, and we have begun the search for his replacement. Each of these appointments will help to drive Hiscox Retail forward in the medium to long term, but as each new CEO gets settled in their new roles, I am expecting growth to be more conservative in the short term.

Hiscox UK & Europe

This division provides personal lines cover – from high-value household, fine art and collectibles to luxury motor – and commercial insurance for small- and medium-sized businesses, typically operating in white collar industries.

These products are distributed via brokers, through a growing network of partnerships and, for some simple risks in the UK, France and Germany, direct to customers. Our schemes business offers insurance solutions to customers with similar risk profiles, for example sports clubs, wedding cars and niche industry associations.

Hiscox UK & Ireland

Hiscox UK & Ireland increased gross premiums written by 11.5% to $799.5 million (2017: $717.1 million), or 7.8% in constant currency, with every region contributing and good growth in most of our product areas.

Cyber remains a bright spot and has grown ahead of budget. The introduction of the EU's General Data Protection Regulation, and no doubt the constant deluge of data breaches that we all read about in the media, are rapidly increasing demand for specialist cover.

Our direct offering is growing well and UK direct reached £100 million of premium this year, helped by a sustained marketing commitment. Building this business has taken time, but the brand we have established and expertise we have embedded is valuable not only to the UK, but also to our other retail operations. It is a model we seek to replicate in our other direct businesses.

The home insurance market remains competitive, with escape of water claims still prevalent and now some subsidence claims after a dry summer. As a result, premiums have increased, and while we try and mitigate the impact of price increases on our customers, we must be disciplined if we are to provide the service that they expect.

In the broker channel, IT change dominated the agenda this year and growth was lower than in previous years. Adapting to our new system with new ways of working has caused some indigestion and had a knock-on effect to our usual standards of service to our brokers and customers. We appreciate their support as we work to get things right. In 2019, our existing broker high net worth business will begin to transition to the new system. We expect growth in the broker channel will continue to be affected as these changes take place, until we reach full operational capability by mid-2019.

Hiscox Europe

Hiscox Europe had another great year. Gross premiums written grew by 17.2% to $322.3 million (2017: $275.0 million), or 11.4% in constant currency, helped by both strong new business and retention. Cyber, classic car, management liability and technology products continue to perform well in Europe and we continue to invest in them.

Germany is now our largest business in terms of premium, with our technology, management liability, motor and cyber products proving most popular. The Frankfurt branch we opened in 2017 is performing well, and having a physical presence in Germany's financial capital is yielding good results. We will extend our regional footprint further during 2019, with new offices in Stuttgart and Berlin.

In Spain our management liability, professional indemnity and cyber products are key growth drivers. We have also experienced strong new business through existing partnerships, by bringing new products to existing distribution channels.

$809.6m

Hiscox USA continues to achieve strong growth, with gross premiums written increasing by 15.4% to $809.6 million (2017: $701.4 million).

Hiscox USA

Our Benelux business has seen good growth in motor, fine art and high-value household where we have benefited from competitors retreating. We launched our cyber and professional indemnity products in Belgium during the year, with promising early signs.

In France, growth has been more muted. After a challenging period in household, we have taken action, implementing a new underwriting and pricing strategy. Cyber and partnerships with financial institutions have performed well, and in motor the partnership we established with Aon has enabled us to materially grow our classic car book.

In most markets, cyber has exceeded our expectations. Our investment in talent and marketing, and the consistency we have introduced in our CyberClear brand is paying off. We have developed a leadership position in Germany and Holland, and Spain has had a very promising response to the cyber product it launched at the start of the year. There is more to do in France, but in time we hope to replicate the success we have had elsewhere.

The shared service centre in Lisbon has grown over the 12 years since it was established, from five people in 2006 to a 400-strong team in 2018. It has created valuable efficiencies for Europe and other parts of our business including Hiscox UK, Hiscox MGA and Group IT now benefit from its support. The roll-out of our 'My Hiscox' broker extranet sites across Europe is progressing to plan, and provides brokers and partners with additional products and convenient self-service features.

The robotic process automation (RPA) that I mentioned last year, which allows us to automate back-end processing and further improve our service levels to brokers and partners, has been rolled out across policy administration, claims and finance and resulted in the automation of 70,000 transactions in 2018. Our focus on IT infrastructure in Europe will continue in 2019, when we will start work to prepare the business for a new core policy, claims, billing and collections system. This will be a similar multi-year undertaking to the work we have done within our UK and US businesses.

Due to the structural changes we have made to our business in readiness for Brexit, Ireland will be reported as part of Hiscox Europe from 2019. One of the upsides of the changes we have implemented is that Hiscox Europe will benefit from greater clarity and attention, with its own Board oversight.

Hiscox International

Hiscox International comprises Hiscox USA, Hiscox Special Risks and Hiscox Asia. It grew by 14.5% to $965.3 million (2017: $843.3 million).

Hiscox USA

Hiscox USA underwrites small- to mid-market commercial risks through brokers, other insurers and directly to businesses online and over the telephone. The business continues to achieve strong growth, with gross premiums written increasing by 15.4% to $809.6 million (2017: $701.4 million).

Our online direct and partnerships division, where the business we write is predominantly for small businesses with one to five employees, continues to be the biggest driver of growth for Hiscox USA. It grew by 43% to reach $206 million. Growing partnership distribution and our commitment to building a direct-to-customer brand are impactful here, and the business will be the first beneficiary of the new policy administration system currently being implemented.

In the broker channel, growth was driven by professional risks and general liability and we benefited from good retention, though new business has been hard fought – especially in the architect and engineers market, where competition is heating up at the lower end of the market. We are maintaining our underwriting and pricing integrity in mid-market cyber, where a maturing US cyber market has led to falling prices and widening cover, and we continue to carefully manage our exposure. Like others in the market, we experienced an increased severity of claims and rate inadequacy for directors and officers' (D&O) for private companies. We have responded with discipline and expect our D&O book to shrink in 2019.

Our new US MGA has now commenced trading, with an initial focus on commercial property. The MGA underwrites on behalf of Hiscox London Market and other Lloyd's syndicates, allowing us to increase our line size and be a more material participant in the market. There is the potential to broaden the MGA's scope over time.

The operational resilience of the business has been boosted by new offices in Las Vegas and Phoenix, which improve our capabilities to serve West Coast customers.

Hiscox Special Risks

Hiscox Special Risks underwrites kidnap and ransom, security risks, personal accident, classic car, jewellery and fine art. Hiscox Special Risks has

The discipline our London Market business has shown over the last three years has paid dividends. Since the end of 2016, the team has walked away from $400 million of challenged business and by the end of 2018 they had succeeded in replacing it.

Hiscox London Market

Hiscox London Market

	2018 $m	2017 $m
Gross premiums written	877.7	749.8
Net premiums earned	551.8	561.6
Underwriting profit/(loss)	68.2	(46.0)
Investment result	13.3	14.5
Foreign exchange and other*	(3.3)	(15.2)
Profit/(loss) before tax	78.2	(46.7)
Combined ratio	89.3	111.6
Combined ratio excluding foreign exchange	89.0	108.7

*Includes impairment.

teams in London, Guernsey, Cologne, Munich, Paris, New York, Los Angeles and Miami.

The business had another good year and delivered gross premiums written of $136.2 million (2017: $127.2 million), an increase of 7.0%. Around half of the business written here are multi-year policies, which impacts on the top line and causes year-to-year volatility in revenues.

We have maintained our market-leading position in kidnap and ransom despite increased competition and ongoing challenges in the rating environment. The Special Risks Underwriting Centre is helping to boost retention and allows underwriters more time to work on complex risks and new business.

Our Security Incident Response product, which responds to a range of security issues such as criminal threats, workplace violence, corporate espionage, mysterious disappearance and cyber extortion, continues to be an important opportunity. It has created a market where none existed previously, and I regularly describe it as the product that every CEO needs. Who do you turn to for help when you face one of these remote, but sadly not unthinkable, events? The product is now available in the UK, USA, Japan, Spain and the Netherlands and we have deployed additional resources to support further growth. The product was recognised with the Innovation Award at Business Insurance magazine's Innovation Awards 2018.

Hiscox Asia

Our brand in Asia, DirectAsia, is a direct-to-consumer business in Singapore and Thailand that sells predominantly motor insurance. Hiscox acquired it in 2014. The business grew its controlled premiums by 32.7% to reach $19.5 million (2017: $14.7 million). This excludes premiums controlled by DirectAsia Thailand, which is currently written via an agency relationship into Hiscox Insurance Company (Bermuda) Limited and reported within Hiscox Re & ILS. From 2019 onwards, premiums controlled by DirectAsia Thailand will be reported within Hiscox Retail, in line with the way the Group reports agency income.

Both Singapore and Thailand remain competitive markets, but focused marketing execution along with product and pricing enhancements in car, motorcycle and travel are helping us to attract and retain more customers. We continue to invest in the business as we strive to reach scale.

We have also expanded our distribution capabilities through commercial partnerships with complementary brands including SingTel, Prudential, DBS, and VICOM in Singapore and KTC in Thailand this year. These partnerships broaden our reach, endorse our brand and help us to grow.

Hiscox London Market

Disciplined cycle management driving excellent results

Hiscox London Market uses the global licences, distribution network and credit rating available through Lloyd's to insure clients throughout the world.

The business has delivered a great result for 2018, increasing gross premiums written by 17.1% to $877.7 million (2017: $749.8 million), or 16.3% in constant currency, with particularly strong growth in property, general liability and cyber. It generated a profit of $78.2 million (2017: loss of $46.7 million) and the combined ratio improved to 89.3% (2017: 111.6%).

The discipline our London Market business has shown over the last three years has paid dividends. Since the end of 2016, the team has walked away from $400 million of challenged business and by the end of 2018 they had succeeded in replacing it with stronger performing business.

The tough action taken in previous years continued in the first part of 2018, when we stopped writing aviation hull and liability, and reshaped our D&O exposure. This work meant we were well positioned for the Lloyd's Decile 10 directive, a crackdown on unprofitable lines by mandating that each syndicate submit plans to address the worst-performing 10% of their business. It made for an interesting business planning process but we had far fewer adjustments to make than some of our peers. We view the action taken by Lloyd's as positive; we all benefit from the Lloyd's brand, rating, central fund and licences, and it is their right to make sure members are competitive. Lloyd's is considered the problem-solver of insurance – its reputation for having the expertise and experience to place complex or unusual risks has been earned through decades of hard work – and we must play our part in helping to retain that.

Our London Market team worked hard to push through rate rises in 2018 and overall rates went up 7%. Notable rate rises for the year were in household and general liability, while terrorism and cyber remain competitive. The 1 January 2019 renewals are most significant for our property and specialty insurance lines, which grew between 5% and 10% year-on-year,

$1.5bn

Assets under management now exceed $1.5 billion after last year's losses.

Hiscox Re & ILS

and in hull and cargo we saw double-digit rate increases at 1 January. Elsewhere rates were flat or up slightly.

As a result of the hurricanes, our property division had another active year for claims but delivered a profit overall. US flood remains a significant opportunity and our FloodPlus products use proprietary technology and advanced analytics to provide better cover at a fairer price for customers, backed by capacity from the flood consortium we lead. FloodPlus performed well in another major US flood event, and during the year we broadened our offering with a FloodPlus Commercial product which has been well received.

Our casualty team focuses on larger company cyber, D&O and general liability. In cyber, although overcapacity is impacting pricing, we remain ambitious and continue to invest in our cyber training programme for brokers which is helping to boost understanding of what remains a complex risk. We have some exposure to the Marriott data loss whose scale and cost reminds us that this is not a risk-free area of activity. The D&O market remains especially challenging, and we significantly refocused our ambitions during the year. Our general liability book continues to grow well and trends look positive. We will expand our capacity in 2019 using consortia with other Lloyd's syndicates.

We have maintained our market share in core lines including terrorism, where our market-leading position continues to stand us in good stead despite the competitive market.

In product recall we remain opportunistic. We responded to the Canadian Cannabis Act – which allows recreational use of marijuana in Canada and has meant that marijuana growers now require product recall cover – with a new product in less than a month, which is just the sort of fleetness of foot and innovation we want to be known for.

The discipline and careful underwriting of our marine and energy team has driven an outstanding performance in these lines, helped too by a low loss experience. In cargo, we are refocusing the portfolio to reduce our overall exposure and lead on more of the business we write.

Our alternative risk team focuses on portfolio business, where we match our capacity and experience with the expertise of underwriters in niche lines that complement our core appetite. It has been a challenging year, with some exposure to the California wildfires albeit within our expected loss experience. The team received recognition for their work at the Reactions London Market Awards 2018, where they were awarded Insurance Team of the Year.

We are making progress with Lloyd's Placing Platform Limited (PPL), the market's move to digital trading. Hiscox bound 45% of all syndicate risks through PPL, exceeding the target of 30% that was mandated by Lloyd's. This is good progress, but there is more to do. In 2019 we will support market moves to make the use of PPL for submissions mandatory, as this is where we will begin to gain the greatest efficiencies.

As previously announced, our 2019 business plan for Lloyd's allows us to underwrite a maximum premium in the year ahead of £1.5 billion for Syndicate 33 (2018: £1.6 billion), a reduction year-on-year as market conditions in 2018 did not tally with our expectations. This gives us sufficient headroom in which to execute our 2019 plans, with some allowance for the unexpected.

Our London Market business is a top quartile performer in Lloyd's and maintaining that position requires active cycle management. In 2019 we will retain our agility, with a particular focus on areas of opportunity within our investment lines.

Hiscox MGA

Hiscox MGA underwrites and distributes products where customers' requirements for capacity exceed Hiscox's own risk appetite, or where the team's distribution focus – both digital and physical – allows us to access business in local markets around the world. It operates out of London, Paris and Miami.

We stopped writing Latin American property facultative reinsurance in the first half of the year, having not seen sufficient rating correction after the loss events of 2017. In space, launch delays have had some short-term top-line impact due to attaching premium moving over to 2019, however we are benefiting from our technical underwriting approach in this line of business and are recognised as a market leader.

Hiscox Re & ILS

Good ILS performance, reinsurance market remains tough

Hiscox Re & ILS comprises the Group's reinsurance teams who are based in London and Bermuda, and ILS activity primarily conducted through our flagship Kiskadee funds. The team underwrites on behalf of Hiscox and third-party capital partners, whether they are insurance companies, other syndicates or capital market investors.

We continued to develop our specialty lines where we see growing opportunity, launching a first-of-its-kind industry loss warranty product in cyber, and in flood, where our FloodXtra product differentiates us.

Hiscox Re & ILS

Hiscox Re & ILS

	2018 $m	2017 $m
Gross premiums written	812.0	700.8
Net premiums earned	257.4	269.3
Underwriting (loss)/profit	(23.2)	4.5
Investment result	12.9	27.9
Foreign exchange and other*	(12.9)	(6.9)
(Loss)/profit before tax	(23.2)	25.5
Combined ratio	116.9	101.3
Combined ratio excluding foreign exchange	112.5	98.9

*Includes finance cost.

Gross premiums written grew 15.9% to $812.0 million (2017: $700.8 million), or 15.0% in constant currency. Property catastrophe reinsurance and specialty reinsurance were the key drivers of growth. A number of natural catastrophes and large claims impacted profits which resulted in a loss of $23.2 million (2017: profit of $25.5 million) and a combined ratio of 116.9% (2017: 101.3%). As explained earlier, the product mix sold to customers responded more to the run of mid-sized catastrophes and large individual losses that occurred in 2018 as compared to the fewer larger catastrophes in 2017. That is the nature of our business – fortuity influences our year-to-year performance, but good underwriting shines through over time.

There was an initial surge of prices in the first quarter following the 2017 hurricane losses, and we were able to write a disproportionate amount of business at that time, but as rate increases tapered off during the course of the year, our growth became more subdued. Overall, we achieved rate increases of 5% for the year.

We continued to develop our specialty lines where we see growing opportunity, launching a first-of-its-kind industry loss warranty product in cyber, and in flood, where our FloodXtra product differentiates us.

During the 1 January 2019 renewal period, we saw overall rate improvements of around 2% across all lines, driven by increases in retro, risk excess, casualty and specialty. As we look towards the Japanese renewals at 1 April and US renewals at 1 June and 1 July, both of which will be loss-affected, we anticipate further pricing correction.

We have seen sustained demand for our ILS offering. Our funds have performed in line with expectations, with the losses of the second half consistent with modelled outcomes. Assets under management now exceed $1.5 billion after last year's losses.

We continue to innovate in ILS and have launched a new fund which allows investors to access insurance lines for the first time. The Kiskadee Latitude fund is supported by a top-tier investor who will access a more diverse insurance and reinsurance portfolio with less focus on pure property catastrophe risk. The fund began underwriting on 1 January 2019, supported by over $100 million.

Claims

We experienced a relatively benign first six months of the year for claims; February's Beast from the East was well within our expected range for a UK weather event, and elsewhere our claims experience was unremarkable. As is the nature of insurance though, anything can happen and it did in the second half of the year, when we experienced a more active environment for both natural catastrophes and large claims.

Hiscox reserved $165 million for Hurricanes Florence and Michael in the USA, and Typhoons Jebi and Trami in the Far East, together with the impact of historic wildfires in California.

In addition, we had some exposure to a number of notable individual claims in cyber, media and marine (including a large marine loss of $13 million). In D&O we experienced a higher severity of claims both in the USA and London Market. The claims trends that I have talked about in Hiscox UK & Ireland – escape of water and subsidence – have also had some effect.

We exercise prudence when it comes to claims reserving, and this approach is evident in reserve releases of $326 million (2017: $324 million) from prior years. This includes favourable experience on the $225 million reserves established for Hurricanes Harvey, Irma and Maria at the end of 2017.

We also announced that the leadership of our claims function is evolving. Jeremy Pinchin, who has held multiple leadership positions during his 13 years at Hiscox, but served throughout as our Group Claims Director, will retire in 2019. When Jeremy joined us in 2005, he was our first Group Claims Director. That year, we paid total claims of around £450 million and had a claims team of less than 50 people. Jeremy has driven the ongoing professionalism of our claim's operations, ensuring its capabilities have scaled in line with our growth, and it is under his leadership that we now have an award-winning claims function, a 250-strong team, and in 2018 paid out £1.2 billion in claims. Paying claims is what we are here for and Jeremy has enabled Hiscox to go from strength-to-strength in this regard. He also made a huge contribution to our industry, particularly after 9/11 when he had the unique role of Special Counsel for Lloyd's and coordinated the market's management of its exposure to the losses arising from September 11.

During his time at Hiscox, Jeremy also served as the first Chief Executive of Hiscox Re; drove the creation of our ILS capability, including naming our funds Kiskadee, a noisy Bermudian bird; served as Chief Executive of Hiscox Bermuda, and as Hiscox Group Company Secretary and General Counsel. I am thankful for his huge and varied contribution to our business during his time at Hiscox.

$69.7m

In 2018 we spent $69.7 million on acquisition and brand-building activity (2017: $69.1 million) with award-winning campaigns such as CyberLive in the UK driving double-digit premium growth in our small business offering.

Marketing

I am pleased that we will continue to benefit from his wisdom as a Non Executive Chairman of Hiscox Special Risks, and as Chairman of the Hiscox Pension Fund.

He is succeeded as Group Claims Director by Grace Hanson. She will be responsible for the strategic direction of Hiscox's claims activities across the Group, working with the standard-bearers for Hiscox's customer promise. We will benefit from Grace's experience, which includes big-ticket property and casualty claims while at Allied World, and volume claims while at Homesite. This combination of knowledge and experience will shape our claims response to the digital era.

Marketing

Our marketing is focused on building a differentiated brand in all our markets to drive value over the short and long term. In 2018 we spent $69.7 million on acquisition and brand-building activity (2017: $69.1 million) with award-winning campaigns such as CyberLive in the UK driving double-digit premium growth in our small business offering. The I'mpossible campaign in the USA continued to run across digital, print, radio and in sponsorship, while in the UK the Hiscox Ever Onwards campaign continued its successful combination of outdoor and radio. Cyber-focused campaigns drove increased awareness of Hiscox across both our business and home insurance customers. We saw great momentum in DirectAsia with new marketing campaigns and distribution partnerships driving new business performance.

Across the Group we activated key partnerships in our core interest areas of art, classic cars and technology, driving awareness and affinity of Hiscox.

Information technology and major projects

A robust modern infrastructure is essential, not only for the business we are today but also the business we want to be. The volume of work taking place around the Group to transform some of our underlying infrastructure is not insignificant, and we are making good progress. As previously stated, cumulatively these projects are increasing our expense ratio by 1%-1.5% in the short term.

The staggered approach we have taken to replacing our core underwriting systems across Hiscox Retail, starting with the UK, has been prudent. Embedding new systems and training our teams to use them takes time, and has had a short-term impact on service levels as our UK business adjusts, but in time we will reap the benefits of new infrastructure. In the USA, we remain on track for our direct and partnerships business to start transitioning to a new system towards the end of 2019. This will create efficiencies for the US business that are essential, given the size of the opportunity ahead of us. In Europe, we have reviewed our IT requirements and made some progress on improving our broker portals and relationship management systems. In time, our European operations will require the same core systems replacement as the UK and USA, so the associated business readiness activities will happen this year.

We completed the replacement of our HR systems across the Group in 2018 and our multi-year programme of finance change initiatives is progressing well. We have also taken positive steps regarding robotics and machine learning, for example, by automating some routine IT service desk tasks. In 2019 we will continue to move forward with our digitisation efforts, looking at broader use of technologies like application programming interfaces (APIs) and robotics that support our push towards portfolio underwriting in the UK, as well as personal lines and claims innovations that benefit our customers.

As we have said before, like others we have also had a plethora of external factors to respond to; Brexit (more on that below), General Data Protection Regulation (GDPR), New York Cybersecurity Regulation, IFRS 17 accounting standards, the Insurance Distribution Directive (IDD) and the updated Senior Managers Certification Regime (SMCR). So as the Chairman has said, 2018 was a year of change and achievement in our operations, with more planned in 2019.

Brexit

Our business is ready for Brexit, even if British politicians are not. We have always said that, for Hiscox, Brexit is structural not strategic. We have built a profitable business in mainland Europe and Ireland over the past 25 years, which serves over 200,000 customers and employs 420 staff. We have put in place the structures needed to continue to serve these customers, as well as those of our customers from elsewhere in the world who have assets or exposures in these territories.

We have created Hiscox SA, a new Luxembourg insurer to carry our retail risks, and will utilise Lloyd's Brussels to insure European Economic Area risks which were previously placed with Lloyd's of London. Adapting to Brexit cost Hiscox approximately $15 million in one-off costs, the majority of which were incurred during 2018, and an expected ongoing cost of $2.4 million per annum. It has also led to an increase in required capital of

We are maturing into a larger and more prominent company, but we strive to retain our entrepreneurial spirit.
Outlook

approximately €100 million, around half of which will moderate over time.

I am proud of the resolve of our teams around the world who have delivered our Brexit solution and I would like to thank them all for their hard work on the project. The Part VII legal process of transferring relevant policies and their associated liabilities from Hiscox Insurance Company to Hiscox SA, as we have just done, is complex, but provides certainty to our customers that we can legally pay all valid claims, even in a hard Brexit scenario. In 2019 we will work with Lloyd's as they complete their Part VII transfer.

Investments

We manage our investment portfolio with two main objectives in mind: providing sufficient liquidity to pay claims and providing capital to support the underwriting business, while generating strong risk-adjusted returns. These objectives were certainly challenged this year.

Our prediction that the end of 2017 would be a turning point in financial markets proved to be correct, and 2018 was a difficult environment for investors. Interest rate rises, volatility spikes and equity price slumps contrasted sharply with the preceding year. Nevertheless, our cautious approach to risk and asset allocation enabled us to generate reasonable returns in turbulent markets.

In keeping with our long-held conservative approach to investing, we were content to accept the returns on offer in the safer corners of the bond markets while maintaining a modest allocation, to equities and hedge funds. As a result of this strategy, our investments made $42.5 million (2017: $112.5 million), before derivatives and fees, a return of 0.7% (2017: 2.0%).

The conventional wisdom that a negative environment for bonds bodes well for equities did not hold true in 2018, with both asset classes underperforming in the majority of markets. In response, we reduced our bond exposure, reducing mark-to-market losses in the process; took refuge in cash, holding more US Dollars than usual; and maintained a low exposure to riskier assets.

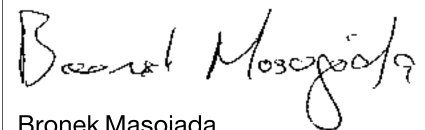
While our investment returns were below our initial expectations, we outperformed our indices through a careful selection of active bond, equity and hedge fund managers.

2019 presents yet more uncertainty, with ongoing political instability in Europe and the potential for recession in the USA. While acknowledging the uncertainty, there are reasons to be optimistic; we have seen a material improvement in yields available and are now investing our US bond portfolio at rates in excess of 3%, something we have not been able to do for nearly a decade. We continue to hold a higher than normal allocation to cash and remain well-placed to invest as opportunities emerge.

Outlook

Our ambition for 2019 is to continue to grow premiums, albeit at a slightly slower pace than 2018. We expect that improving pricing as a result of Lloyd's Decile 10 and our ongoing portfolio optimisation will lead to more insurance profit, with higher interest rates driving better investment returns. We will continue to invest in our underlying infrastructure and our brand. All of this will help propel our business forward.

We are maturing into a larger and more prominent company, but we strive to retain our entrepreneurial spirit. We were promoted to the FTSE 100 at the end of 2018, the consequence of our past endeavours. It was a moment of quiet satisfaction, but more of trepidation. More people will have more opinions on what we should or shouldn't do. We are alive to the responsibilities, but will seek to live up to our ethos of challenging convention. We are fortunate that in many of our chosen areas, we are still small players with plenty of opportunity ahead of us. People, brand, products and strategic ambition differentiate us and we will continue to nurture them in the year ahead to the benefit of customers, staff and shareholders.



Bronek Masojada
25 February 2019

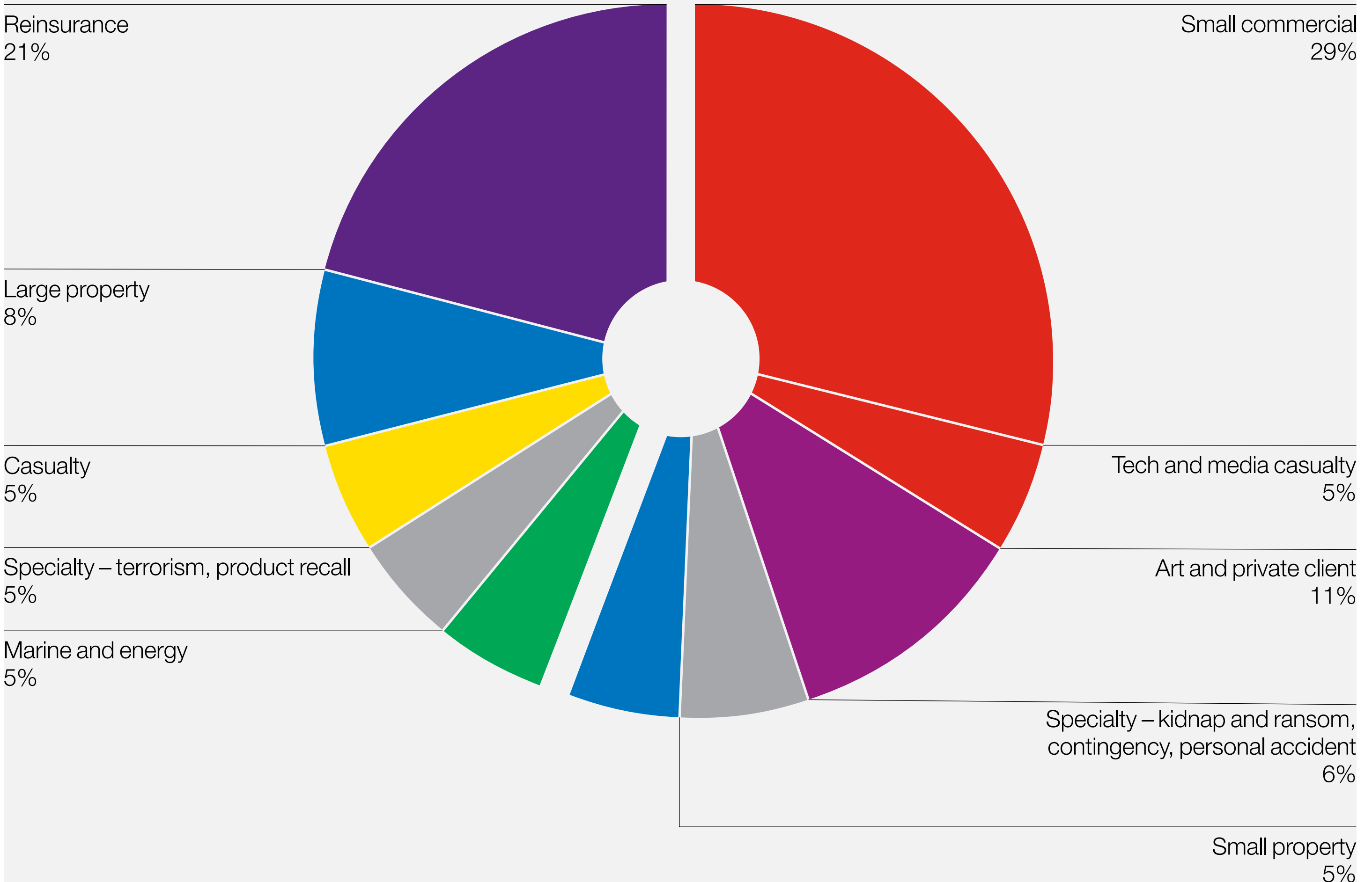
Building a balanced business

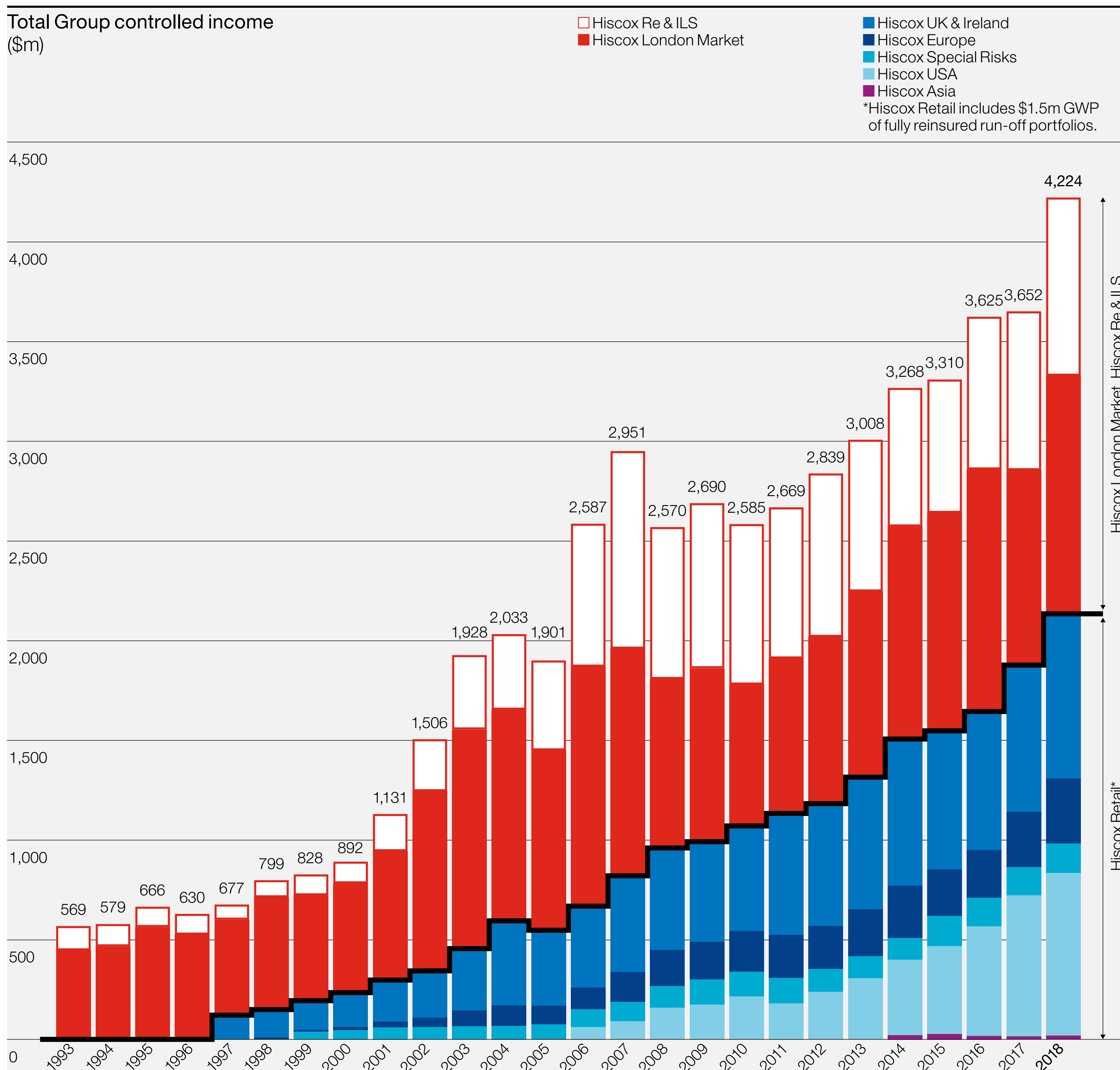
Hiscox enjoys a symbiotic relationship between more catastrophe-exposed, globally traded business, and comparatively less volatile, smaller premium retail business which gives us opportunities throughout the insurance cycle.

Total Group controlled income for 2018
100% = $4,224 million

Big-ticket business
- Larger premium, globally traded, catastrophe-exposed business written mainly through Hiscox London Market and Hiscox Re & ILS.
- Shrinks and expands according to pricing environment.
- Excess profits allow further investment in retail development.

Retail business
- Smaller premium, locally traded, relatively less volatile business written mainly through Hiscox Retail.
- Growth between 5-15% per annum.
- Pays dividends.
- Specialist knowledge differentiates us and investment in brand builds strong market position.
- Profits act as additional capital.




Total Group controlled income
($m)
Hiscox Re & ILS
Hiscox London Market
Hiscox UK & Ireland
Hiscox Europe
Hiscox Special Risks
Hiscox USA
Hiscox Asia
*Hiscox Retail includes $1.5m GWP of fully reinsured run-off portfolios.
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2018
Hiscox London Market, Hiscox Re & ILS
Hiscox Retail*

Actively managed business mix

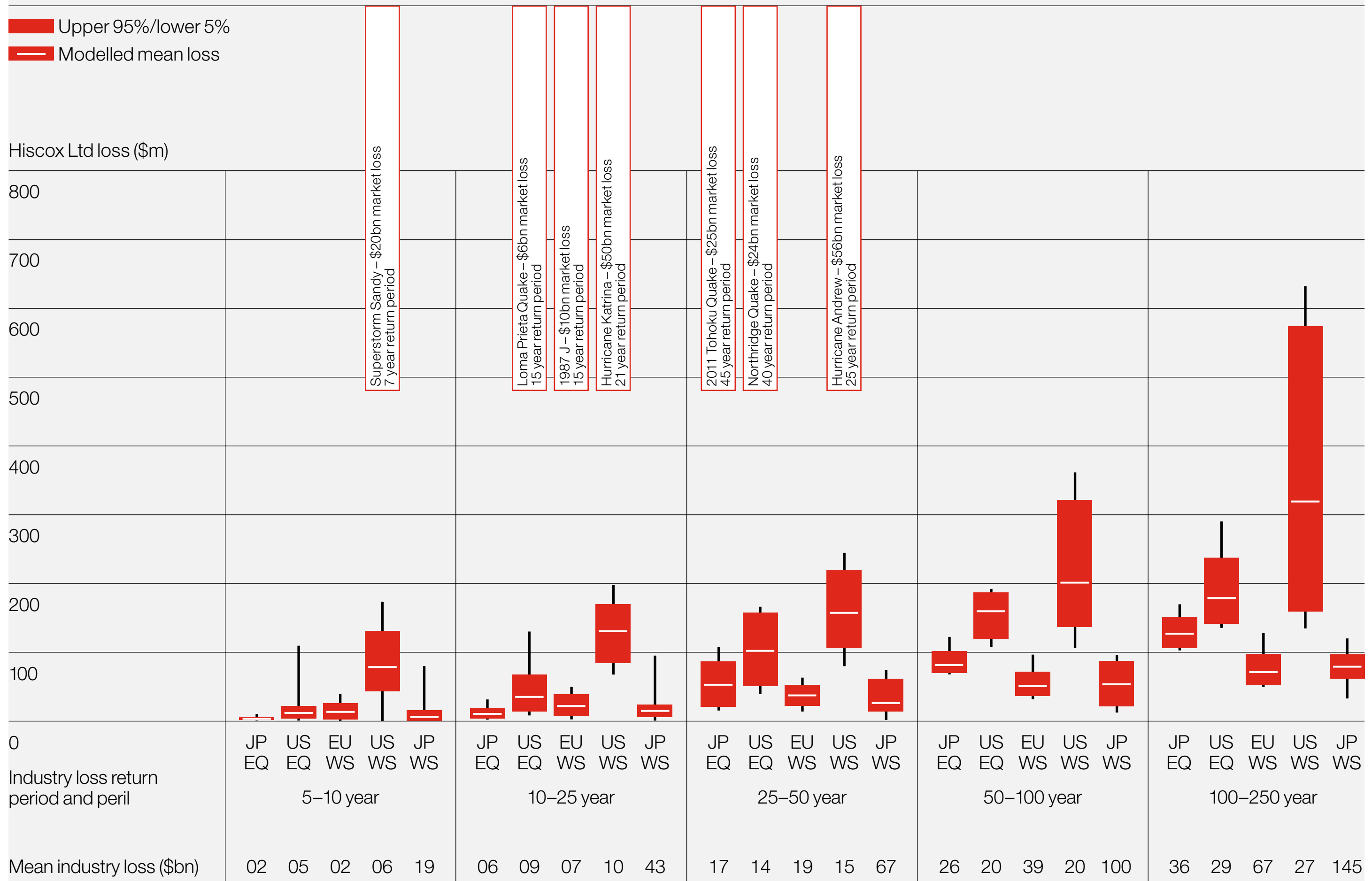
Total Group controlled premium 2018: $4,224 million
(Period-on-period in local currency)

Small commercial	Reinsurance	Property	Art and private client	Specialty	Global casualty	Marine and energy
+13.7%↑	+12.9%↑	+51.3%↑	+4.9%↑	-4.3%↓	+17.2%↑	+7.5%↑
$1,452m	$894m	$554m	$469m	$442m	$215m	$198m
Professional liability Errors and omissions Private directors and officers' liability Cyber Commercial small package Small technology and media Healthcare related Media and entertainment	Non-marine Marine Aviation Casualty Specialty	Commercial property Onshore energy USA homeowners Managing general agents International property	Home and contents Fine art Classic car Luxury motor Asian motor	Kidnap and ransom Contingency Terrorism Product recall Personal accident Aerospace Contractors' equipment FTC	Public D&O Professional indemnity Large cyber General liability	Cargo Marine hull Energy liability Offshore energy Marine liability

Actively managed key underwriting exposures

Boxplot and whisker diagram of Hiscox Ltd net loss ($m) for certain modelled losses

January 2019



This chart shows a modelled range of net loss the Group might expect from any one catastrophe event.
The white line between the bars depicts the modelled mean loss.

The return period is the frequency at which an industry insured loss of a certain amount or greater is likely to occur.
For example, an event with a return period of 20 years would be expected to occur on average five times in 100 years.

JP EQ – Japanese earthquake, US EQ – United States earthquake, EU WS – European windstorm, US WS – United States windstorm, JP WS – Japanese windstorm

Realistic disaster scenarios, Hiscox Ltd

The table below presents selected realistic disaster scenarios based on our book of business in force at 1 January 2019 and industry data. Given the nature of the risks underwritten, the loss estimates may be materially different from those that arise depending on the size and nature of the event.

	Gross loss $m	Net loss $m	Gross loss as a % of total equity	Net loss as a % of total equity	Net loss as a % of insurance industry loss	Industry loss size $bn	Return period years
Japanese earthquake	963	154	41.6	6.7	0.3	50	240
Japanese windstorm	485	101	20.9	4.4	0.7	15	100
Gulf of Mexico windstorm	1,757	184	75.8	7.9	0.2	107	80
Florida windstorm	1,340	224	57.9	9.7	0.2	125	100
European windstorm	586	86	25.3	3.7	0.3	30	200
San Francisco earthquake	1,340	207	57.8	8.9	0.4	50	110

Capital

Hiscox monitors its capital requirements based on external risk measures and internal risk appetite.

Capital management

The Board is responsible for monitoring the capital strength of the Hiscox Group and ensuring that its insurance carriers are suitably capitalised for regulatory and rating purposes, taking into account future needs including growth where opportunities arise.

Given our capital strength and balance sheet resilience, we continue to maintain a progressive core dividend policy. The Group has proposed to increase the final dividend by 5.1% to 28.6¢, resulting in a full-year ordinary dividend of 41.9¢ (2017: 39.8¢), up 5.2%. Our focus on efficient capital management means the business remains well positioned to support growth in areas expected to be profitable.

Capital requirements

Monitoring of the Group's capital requirements is based on both external risk measures, set by regulators and rating agencies, and our own internal guidelines for risk appetite. A full description of the requirements set by the regulators for the most significant insurance carriers is included in note 3.3 to the financial statements. A brief explanation of the primary internal and external capital constraints at Group level is given below, and presented in the chart on page 23.

The Group measures its capital requirements against its available capital. Available capital is defined by the Group as the total of net tangible asset value and subordinated debt.

The subordinated debt issued by the Group is hybrid in nature, which means it counts towards regulatory and rating agency capital requirements. At 31 December 2018 available capital was $2,463 million (2017: $2,553 million), comprising net tangible asset value of $2,113 million (2017: $2,182 million) and subordinated debt of $350 million (2017: $371 million).

The Group can source additional funding from revolving credit and Letter of Credit (LOC) facilities. Standby funding from these sources comprised $800 million at 31 December 2018 (2017: $500 million), of which $50 million was utilised at 31 December 2018 (2017: $10 million).

Rating agencies

Our ability to attract business, particularly reinsurance, is dependent upon the maintenance of appropriate financial strength ratings from the leading rating agencies: A.M. Best, S&P and Fitch. These ratings are assigned based on a range of factors, including business model, risk management framework and financial strength. They are assigned individually to the insurance carriers of the Group, but capital adequacy is monitored primarily by the rating agencies at the consolidated Group level.

A.M. Best, S&P and Fitch capital models calculate capital adequacy by measuring available capital, after making various balance sheet adjustments, and comparing it with required capital, which incorporates charges for premium, reserve, investment and catastrophe risk. Our interpretation of the results of each of these models indicates we are comfortably able to maintain our current ratings as set out in note 3.3 to the financial statements. The rating agency requirements shown in the chart on page 23 are consistent with the Group's own internal projections of rating agency capital requirements.

Group regulators

As a Bermudian-registered holding company, the Group is regulated by the Bermuda Monetary Authority (BMA) under the Bermuda Group Supervisory Framework. The BMA requires Hiscox to monitor its Group solvency capital requirement and provide a solvency return in accordance with the Group Solvency Self Assessment framework (GSSA), including an assessment of the Group's Bermuda Solvency Capital Requirement (BSCR). The BSCR model applies factors to premium, reserves and assets/liabilities to determine the minimum capital required to remain solvent throughout the year.

The GSSA is based on the Group's own internally assessed capital requirements and is informed by the Group-wide Hiscox Integrated Capital Model (HICM) which, together with the BSCR, forms part of the BMA's annual solvency assessment. The HICM provides a consistent view of capital requirements for all segments of the business and at Group level.

We are also required to publish a Financial Condition Report (FCR), which sets out details of the measures governing the Group's business operations, corporate governance framework, solvency and financial performance. The FCR is also intended to provide additional information about the Group's business model, enabling the public to make an informed assessment on whether the business is run in a prudent manner. A copy of our FCR can be found at www.hiscoxgroup.com/about-hiscox/group-policies-and-disclosures

Internal capital requirements

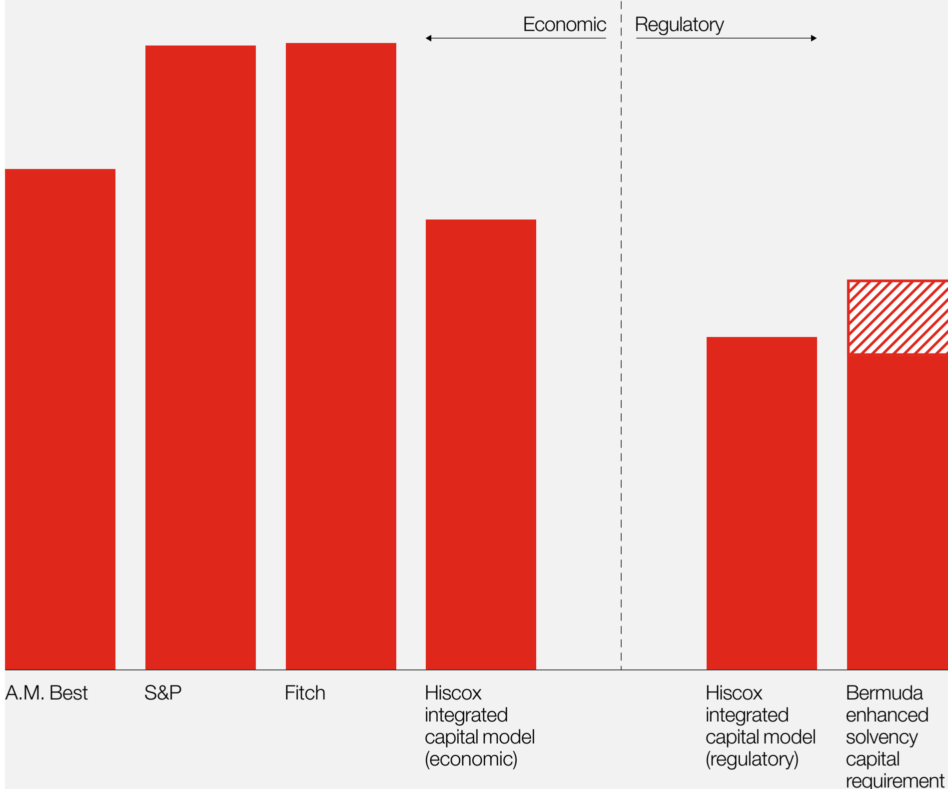
The Group sets risk limits and tolerances that reflect the amount of risk it is willing to accept. To ensure good risk management, our current exposure by key risk type is

$2,463m

Available capital as at 31 December 2018.

Our focus on efficient capital management means the business remains well positioned to support growth in areas expected to be profitable.

Capital management



Rating agency assessments shown are internal Hiscox assessments of the agency capital requirements on the basis of year end 2018 results. Hiscox uses the internally developed Hiscox integrated capital model to assess its own capital needs on both a trading (economic) and purely regulatory basis. All capital requirements have been normalised with respect to variations in the allowable capital in each assessment for comparison to a consistent available capital figure. The available capital figure comprises net tangible assets and subordinated debt.

monitored against these predefined measures throughout the year.

The largest driver of our capital is underwriting risk. The Group manages the underwriting portfolio so that in a one-in-200 aggregate bad year it will lose no more than 12.5% of core capital plus 100% of buffer capital ($135 million) with an allowance for expected investment income. A market loss at this remote return period would be very large indeed and would be expected to bring about increases in the pricing of risk. Our capital strength and financial flexibility following this scenario means the Group would be well positioned to take advantage of any opportunities that might arise. After the payment of the final dividend on 12 June 2019, the available capital will reduce to approximately $2,382 million, comfortably meeting the current regulatory, rating agency and internal capital requirements. Our estimate of the year-end 2018 BSCR solvency ratio is 210%. The Group continues to operate with a strong solvency position. In addition, each of the respective insurance carriers holds appropriate capital positions on a local regulatory basis.

The BMA is planning to phase in changes to the BSCR over a three-year period, starting at the end of 2019, which is expected to reduce the BSCR solvency ratio. The Group expects to maintain an appropriate margin of solvency after these changes have taken effect. The total impact of this change once it has been fully phased in, is shown in the chart on the left. It is expected to reduce the BSCR solvency ratio by approximately 15%-20%.

Group financial performance

Good underwriting performances in our retail and London Market businesses helped mitigate the impact of natural catastrophes, large losses and investment market volatility.

The Hiscox Group delivered profit before tax for the year of $137.4 million (2017: $39.7 million), or $151.1 million (2017: $120.6 million) excluding foreign exchange gains/losses.

This is a good result considering the Group reserved $165 million for natural catastrophes and large losses in the second half of the year. The Group's change in functional currency to US Dollars at the beginning of 2018 had the desired effect, significantly reducing the impact of foreign exchange movements during the period. The investment return of 0.7% (2017: 2.0%) was materially impacted by mark-to-market adjustments on the bond portfolio due to rising interest rates in the USA, as well as volatility in investment markets. The Group recorded a post-tax return on equity of 5.6% (2017: 1.5%) and earnings per share of 45.1¢ (2017: 12.0¢).

Net asset value per share decreased by 1.9% to 819.1¢ (2017: 835.1¢), with net tangible asset value at 746.4¢ (2017: 769.5¢). The Board has proposed a final dividend of 28.6¢ per share, to be paid on 12 June 2019 to shareholders on the register at 10 May 2019, taking the total ordinary dividend per share for the year to 41.9¢, an increase of 5.2% (2017: 39.8¢). The Group maintains a progressive dividend policy.

Gross premiums written of $3.8 billion grew 14.9% year-on-year, or 13.2% in constant currency. Hiscox Retail continued its strong growth trajectory, up 13.7% for the year, and accounting for 55% of the Group's gross premiums written. Hiscox London Market returned to growth in 2018, up 17.1%, and Hiscox Re & ILS grew by 15.9%. The Group's combined ratio was 94.9% (2017: 99.9%), or 94.4% (2017: 98.8%) excluding the impact of foreign exchange.

The underwriting performance for each operating segment is detailed as follows.

Hiscox Retail

Hiscox Retail accounts for 55% (2017: 56%) of the Group's gross premiums written at $2,087.1 million (2017: $1,835.4 million). Gross premiums written for Hiscox UK & Ireland were up by 11.5% at $799.5 million (2017: $717.1 million), or 7.8% in constant currency. Hiscox Europe's gross premiums written saw very healthy growth, up 17.2% to $322.3 million (2017: $275.0 million), or 11.4% in constant currency. Hiscox USA's strong growth continued, with gross premiums written up 15.4% to $809.6 million (2017: $701.4 million). Gross premiums written within Hiscox Special Risks increased to $136.2 million (2017: $127.2 million), up 5.5% in constant currency, and DirectAsia grew premiums by 32.7%, contributing $19.5 million of gross premiums written (2017: $14.7 million).

Overall the net combined ratio improved to 93.6% (2017: 94.6%), with the net claims ratio decreasing to 43.8% (2017: 45.2%) despite an increase in losses for Hiscox USA, and increased operational expenditure on major projects which saw the expense ratio increase slightly to 49.8% (2017: 49.3%). Profit before tax was $136.0 million (2017: $141.6 million). The underwriting result, excluding the impact of foreign exchange, finance costs and investments, improved by 11.1% to $125.4 million (2017: $112.8 million). This result highlights the quality of our retail underwriting and the balance that the more stable earnings of our retail businesses brings to our more volatile, catastrophe-exposed big-ticket lines.

Hiscox London Market

Gross premiums written increased by 17.1% to $877.7 million (2017: $749.8 million), as the business took advantage of a second successive year of rate improvement, finding opportunities in property and specialty lines. This represents a 16.3% increase (2017: 23.1% decline) in constant currency. The net claims ratio improved to 46.0% (2017: 70.1%) as the business delivered a strong performance in the face of significant market losses. This is reflected in the combined ratio which, excluding foreign exchange movements, improved to 89.0% (2017: 108.7%). The expense ratio rose to 43.0% (2017: 38.6%) due to an increase in the proportion of higher-commission property binder business being written, as well as Group project expenditure. The profit before tax for the year was $78.2 million (2017: loss of $46.7 million) or, excluding foreign exchange gains, $80.9 million (2017: loss of $31.5 million).

Hiscox Re & ILS

Gross premiums written increased by 15.9% to $812.0 million (2017: $700.8 million), or 15.0% in constant currency. The claims ratio increased to 83.8% (2017: 71.0%) as the business was impacted by significant catastrophes and large losses in the specialty book. The quota share arrangements with Syndicate 6104 remained in place. As a result, the net combined ratio excluding foreign exchange movements increased to 112.5% (2017: 98.9%). The expense ratio increased to 28.7% (2017: 27.9%), again due to Group project expenditure. The result for the division was a loss of $23.2 million (2017: profit of $25.5 million).

Hiscox Corporate Centre

The central investment portfolio returned $2.4 million (2017: $32.9 million) during the year. As the Corporate Centre holds a significant proportion of US Dollar assets to support the underwriting activities

The Group's change in functional currency to US Dollars at the beginning of 2018 had the desired effect, significantly reducing the impact of foreign exchange movements during the period.

94.4%

Combined ratio excluding foreign exchange impact.

of the managed syndicates, foreign exchange movements resulted in a loss of $13.7 million (2017: loss of $80.7 million). The impact was moderated significantly by the Group's change in functional currency to US Dollars at the beginning of 2018. As a result, the loss before tax was $53.6 million (2017: loss of $80.7 million).

Cash and liquidity

The Group's primary source of liquidity is from premium and investment income. These funds are used predominantly to pay claims, expenses, reinsurance costs, dividends and taxes, and to invest in more assets.

During the year, the Group completed a $380 million bond issuance. This further optimised the Group's liquidity position, giving us the strategic flexibility to react to changing market conditions and seize profitable growth opportunities as they arise.

The Group returned $107.2 million of capital to its shareholders in 2018 (2017: $97.9 million). Inflows for the year were $442.9 million (2017: inflow of $3.0 million).

The Group paid $24.2 million of tax during the year compared with $43.4 million in 2017. The 2017 payment includes amounts paid for the more profitable 2016 financial year.

The Group had net cash outflows from investing activities of $59.6 million (2017: inflow of $3.3 million), with continued underwriting software development. Marketing expenses remained a major component of our expense base at $69.7 million during the year (2017: $69.1 million).

Group key performance indicators

	2018					2017				
	Hiscox Retail	Hiscox London Market	Hiscox Re & ILS	Corporate Centre†	Total	Hiscox Retail	Hiscox London Market	Hiscox Re & ILS	Corporate Centre	Total
Gross premiums written ($m)	2,087.1	877.7	812.0	1.5	3,778.3	1,835.4	749.8	700.8	–	3,286.0
Net premiums written ($m)	1,874.5	522.9	241.5	(57.4)	2,581.5	1,674.3	484.9	243.8	–	2,403.0
Net premiums earned ($m)	1,821.9	551.8	257.4	(57.4)	2,573.7	1,585.3	561.6	269.3	–	2,416.2
Investment result ($m)	9.5	13.3	12.9	2.4	38.1	29.5	14.5	27.9	32.9	104.8
Profit/(loss) before tax ($m)	136.0	78.2	(23.2)	(53.6)	137.4	141.6	(46.7)	25.5	(80.7)	39.7
Claims ratio (%)	43.8	46.0	83.8	–	48.5	45.2	70.1	71.0	–	54.9
Expense ratio (%)	49.8	43.0	28.7	–	45.9	49.3	38.6	27.9	–	43.9
Foreign exchange impact (%)	–	0.3	4.4	–	0.5	0.1	2.9	2.4	–	1.1
Group combined ratio (%)	93.6	89.3	116.9	–	94.9	94.6	111.6	101.3	–	99.9
Financial assets and cash* ($m)					6,261.9					5,957.1
Other assets ($m)					4,584.4					3,772.7
Total assets ($m)					10,846.3					9,729.8
Net assets ($m)					2,317.1					2,368.4
Net asset value per share (¢)					819.1					835.1
Net tangible asset value per share (¢)					746.8					769.5
Adjusted number of shares in issue (m)					282.9					283.6

*Excluding derivative assets and insurance-linked securities funds.
†Includes a run-off casualty portfolio following the completion of a loss portfolio transfer reinsurance treaty effective from 2018 ceding any future payments on losses arising from claims developments related to policies written from 2010 to 2016, with premiums earned of $(57.4) million and claims adjustment expenses net of reinsurance of $57.5 million.

Group investments

Turbulent investment markets in 2018 have rewarded our cautious approach to risk and asset allocation.

The Group's invested assets at 31 December 2018 totalled $6.3 billion (2017: $6.0 billion). The increase was largely as a result of the $380 million bond issuance in the first quarter, which is discussed in more detail in the Group financial performance section on page 25. The size of the portfolio was otherwise broadly unchanged over the period. The investment result, excluding derivatives and fees, was $38.0 million (2017: $104.8 million), a return of 0.7% (2017: 2.0%).

2018 proved to be very different to the preceding year. Disappointing overall asset performance was driven largely by concerns around the tightening of USA monetary policy. In the first quarter this led to increased market volatility depressing equity markets. In the fourth quarter, comments by US Federal Reserve Chairman Jerome Powell again drove equity markets down and also, this time, bond yields.

2018 also saw the fortunes of US and European bond markets diverge. The US economy benefited from the long-term impacts of its quick and decisive action following the 'credit crunch' and the short-term impacts of the President's recent fiscal injection. As a result, USA one-month interest rates increased by almost 1% to reach 2.5%, while two-year government rates ultimately rose by 0.6% to 2.5% after a strong end to the year. By contrast, UK and European economies were constrained by widespread political uncertainty including Brexit and Italy's budgetary brinkmanship with the EU. UK two-year government bond yields rose by only 0.3% and German two-year bund yields were unchanged.

Rising interest rates, while clearly beneficial to our portfolios over the medium term, do negatively impact short-term performance as increasing rates lead to lower bond values and mark-to-market losses. Returns from bond coupon income were strong and we expect to recover the mark-to-market losses as bonds mature. We are now re-investing cash at rates over 3% for the first time since 2009.

The overall return on our bond portfolio was 0.7%, with our 70% holding of US Dollar bonds returning 0.9%. Given our underwriting mix, we are required to hold Sterling and Euro bonds, which underperformed our US Dollar holdings, generating returns of 0.4% and 0.2% respectively. Over the year, we reduced the maturity of our portfolios which limited our mark-to-market losses. This had no material adverse impact on our expected income. We therefore see our bond return as quite strong in the circumstances.

While our overall asset performance suffered in the conditions, the impact was mitigated by our cautious approach to asset allocation which saw us hold an overweight portion of 20% in cash – one of the best performing asset classes in 2018 – and an underweight position of only 7% in risk assets. This action was timely, as 2018 was a particularly difficult year for risk assets as global equities, UK equities and hedge funds all struggled.

Investment return breakdown ($m)

	2018	2017	2016
Cash and bond income (net of fees)	97	75	68
Bond mark-to-market	-31	-23	4
Risk asset return	-28	53	23
Total	38	105	95

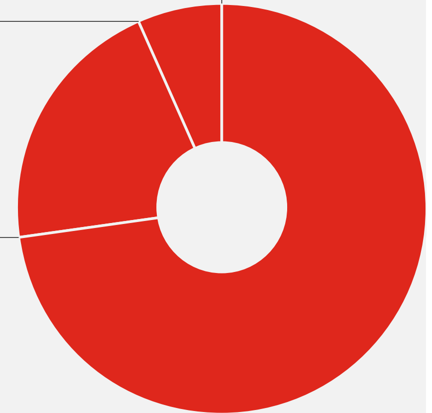
In addition to our sensible, tactical asset allocation position, our selection of asset managers benefited our return; each asset class outperformed its respective index. 2018 has demonstrated the value of active management in minimising losses in volatile markets, with about half of our asset return arising from the outperformance of our active managers. Nevertheless, we see value in both active and passive approaches and will utilise whichever best suits Hiscox's interests.

Clearly, markets have entered a new phase and we expect to have to weather more bouts of volatility as growth slows and liquidity is drained from the market. In 2018, we started to restructure our risk assets to reduce volatility while maintaining return. We will continue this process in 2019, again choosing strong, diversifying risk asset managers and using more sophisticated quantitative techniques to manage our positions. We have also started to incrementally increase the risk in our bond portfolios by investing in shorter-dated, high-quality non-government bonds. This will increase our medium-term expected return with only a modest increase in risk.

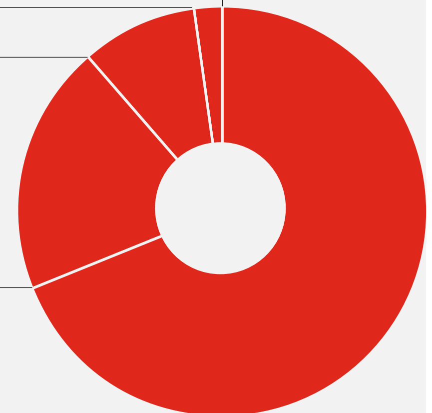
We remain underweight on all risk metrics, maintaining a prudent stance in the face of volatility to support the core Hiscox business. Nevertheless, we remain ready for a healthier investment climate.

2019 will also see an increase in focus on responsible investing as well as a specific focus on the impact of our investments on climate change.

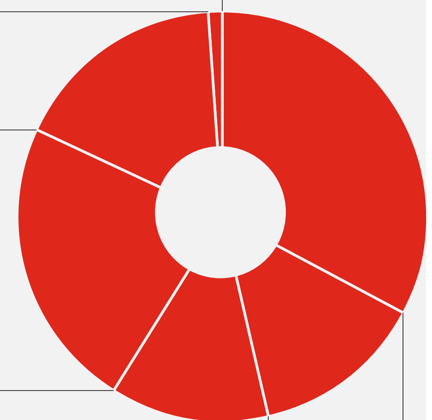
Asset allocation



Bond currency split



Bond credit quality



Additional performance measures (APMs)

APMs are commonly used measures to allow comparison across peer companies.

The Group uses, throughout its financial publications, additional performance measures (APMs) in addition to the figures that are prepared in accordance with International Financial Reporting Standards (IFRS). The Group believes that these measures provide useful information to enhance the understanding of its financial performance. These APMs are: profit excluding foreign exchange gains/(losses), premium growth in local currency, combined claims and expense ratios, return on equity, net asset value per share and reserve releases. These are common measures used across the industry, and allow the reader of our Annual Report and Accounts to compare across peer companies. The APMs should be viewed as complementary to, rather than a substitute for, the figures prepared in accordance with IFRS.

Profit excluding foreign exchange gains/(losses)

This represents the profit for the period after deducting foreign exchange gains or adding back foreign exchange losses in the relevant period. This enables the reader of these financial statements, and the Group, to measure the comparability of underlying profitability without the foreign exchange volatility. To obtain the value, the reader of these financial statements should remove the foreign exchange gains/(losses), as identified in the income statement, from the profit for the period.

Premium growth in local currency

Gross premiums written, as reported in the consolidated income statement, is measured in the underlying currency and compared to prior years on a constant currency rate basis. This eliminates the impact exchange fluctuations have on the result and therefore allows a direct comparison between years. This is performed on a business unit basis and gives an accurate indication of premium growth compared to prior years.

Combined claims and expense ratios

The combined claims and expense ratios are common measures enabling comparability across the insurance industry that measure the relevant underwriting profitability of the business by reference to its costs as a proportion of its net earned premium. The Group calculates the combined ratio as if we owned all of the business, including the 27.4% of Syndicate 33 that the Group does not own (Group controlled income). The Group does this to enable comparability from period to period as the business mix may change in a segment between insurance carriers, and this enables the Group to measure all of its underwriting businesses on an equal measure. The calculation is discussed further in note 4, operating segments. The combined ratio excluding foreign exchange gains is calculated as the sum of the claims ratio and the expense ratio.

Return on equity (ROE)

As is common within the financial services industry, the Group uses ROE as one of its key performance metrics. While the measure enables the Company to compare itself against other peer companies in the immediate industry, it is also a key measure internally where it is used to compare the profitability of business segments, and underpins the performance-related pay and shared-based payment structures, as discussed within the remuneration policy on pages 84-93. The ROE is shown in note 6, along with an explanation of the calculation.

Net asset value (NAV) per share

The Group uses NAV per share as one of its key performance metrics, including using the movement of NAV per share in the calculation of the options vesting of awards granted under PSP from 2018 onwards. This is a widely used key measure for management and also for users of the financial statements to provide comparability across peers in the market. NAV per share is shown in note 5, along with an explanation of the calculation.

Reserve releases

Reserve releases are a measure of favourable development on claims reserves that existed at the prior balance sheet date. It enables the users of the financial statements to compare and contrast the Group's performance relative to peer companies. The Group maintains a prudent approach to reserving, to help mitigate the uncertainty within the reserve estimates. The release is calculated as the movement in ultimate losses on prior accident years between the current and prior-year balance sheet date, as shown in note 23, as the result of better than expected outcomes of the estimates booked at the prior period close.

A specialist approach

Taking the easiest and most obvious route is always tempting. The problem is that easy, obvious routes tend, by their very nature, to be extremely crowded. In the insurance industry, as in so much of life, the greatest rewards are often to be gained by heading off along paths that are less well trodden and less clearly signposted.

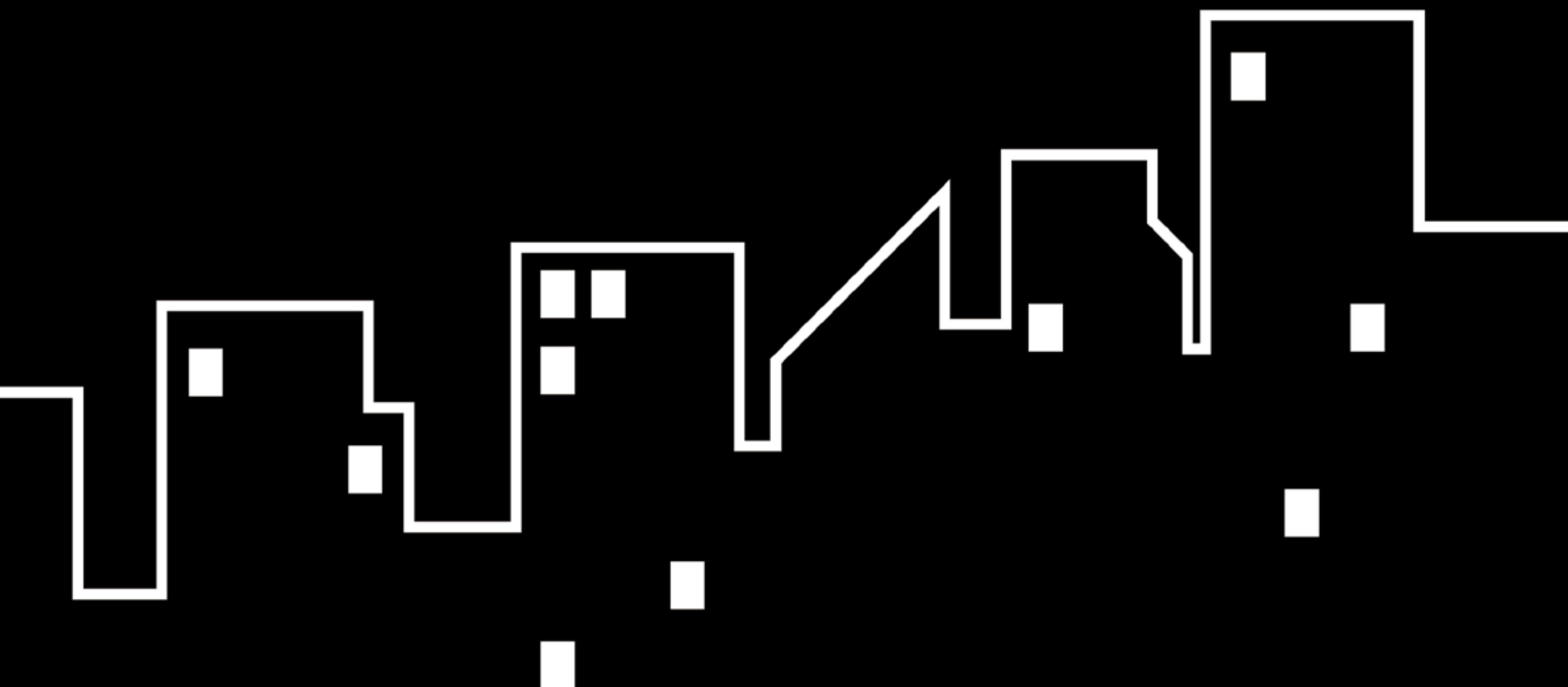
Fine art, flood, small business, security incident response, cyber. These areas, in which Hiscox currently seeks to excel, are all either highly specialist, rapidly developing or else prone to fluctuations in character and scale. In some, such as fine art, we have deep foundations to build on; in others we are still relative newcomers. But to be successful in any of these complex or fast-moving marketplaces, it is essential that we invest in people, infrastructure and digital solutions.

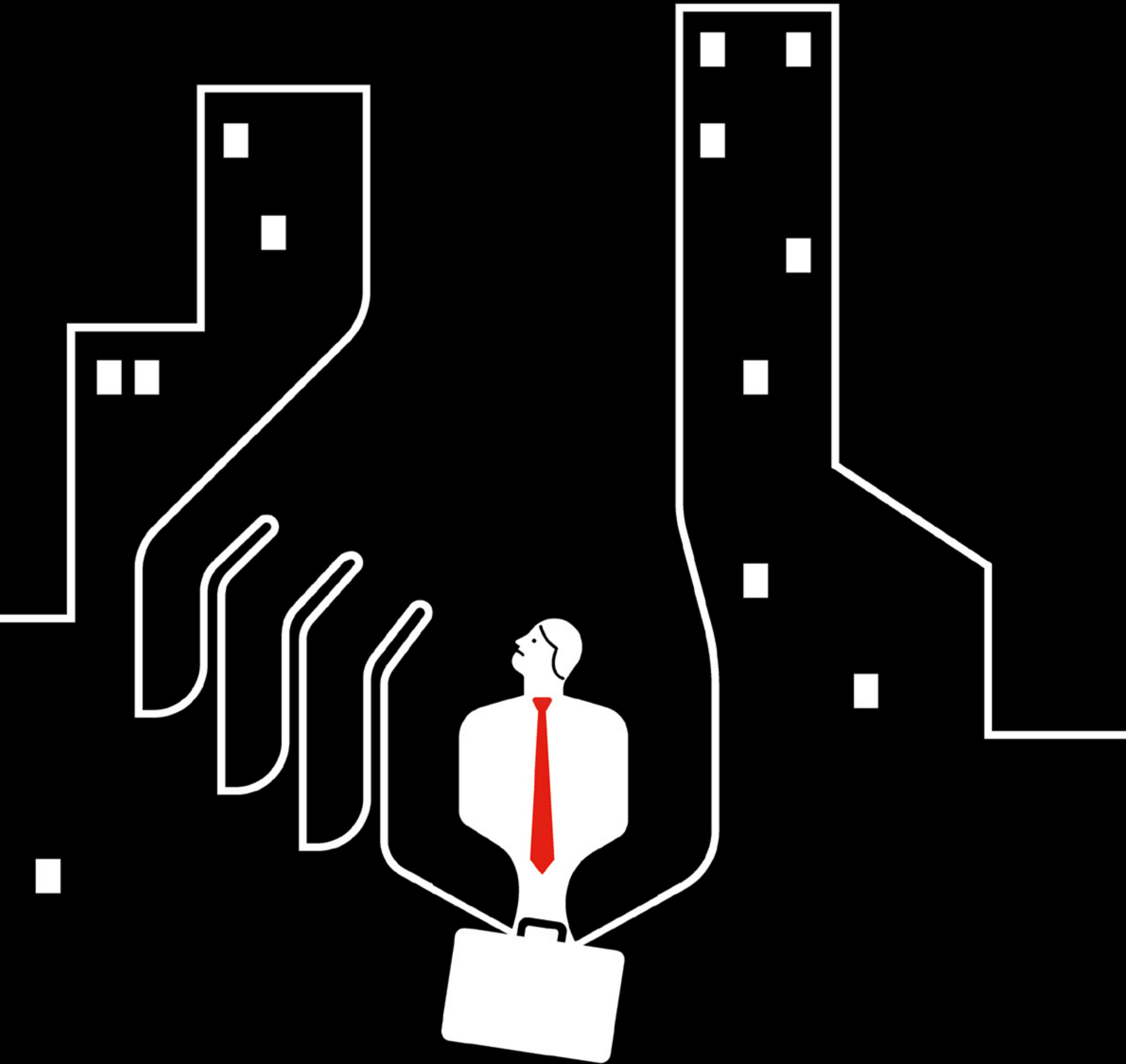
The challenging character of this terrain requires us to be as agile as possible, with a flexibility and fleetness of foot that allows us to quickly enter new markets or respond rapidly to changes in more established ones. Our culture has to be one that encourages innovation, personal development and thoughtful risk-taking, that embraces new ideas while understanding that bringing them to fruition takes time, patience and careful analysis.

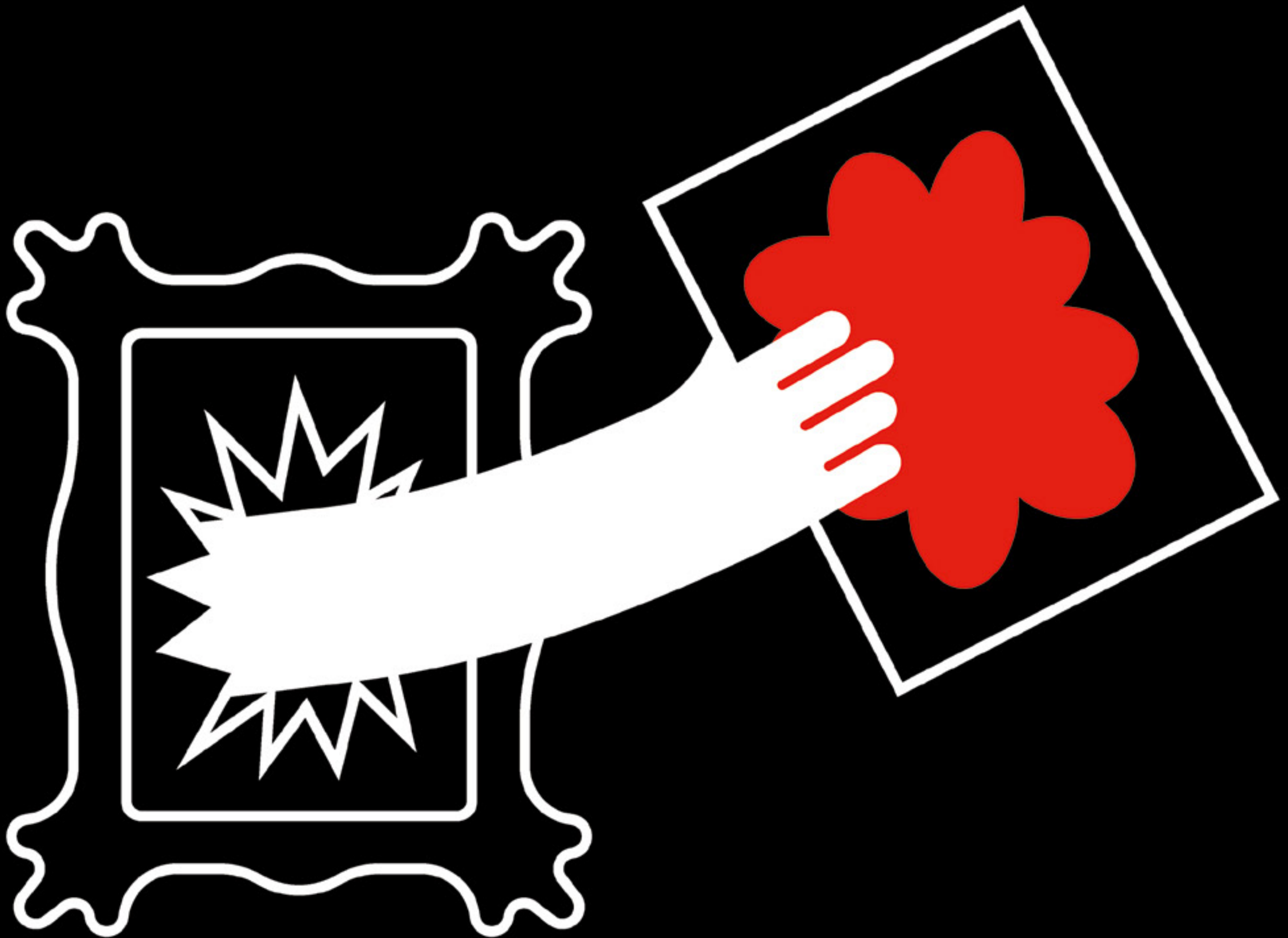
We are one of the few insurers to cover one-man-bands, right up to the largest multinationals, and we try to bring that spirit of versatility to everything we do, even as the landscape shifts.

Security Incident Response (SIR)

Global businesses face a myriad of security and integrity risks, and nowhere in the world can security be taken for granted. The threats presented by crime, terrorism, corruption and political instability are increasingly complex in nature and frequently transcend international borders. Every business with a global presence, with offices in any major city centre on any continent, or whose employees are expected to travel widely, needs to understand and manage these hazards in order to protect their people, operations and reputation. Hiscox launched its SIR product in 2017 to help large, multinational organisations address these challenges through our experience and that of our partner, Control Risks, an international risk management and security consultancy. It allows a response to be activated at the first suspicion of a developing risk, meaning executives and their senior teams can get ahead of fast-moving events before they become a crisis.





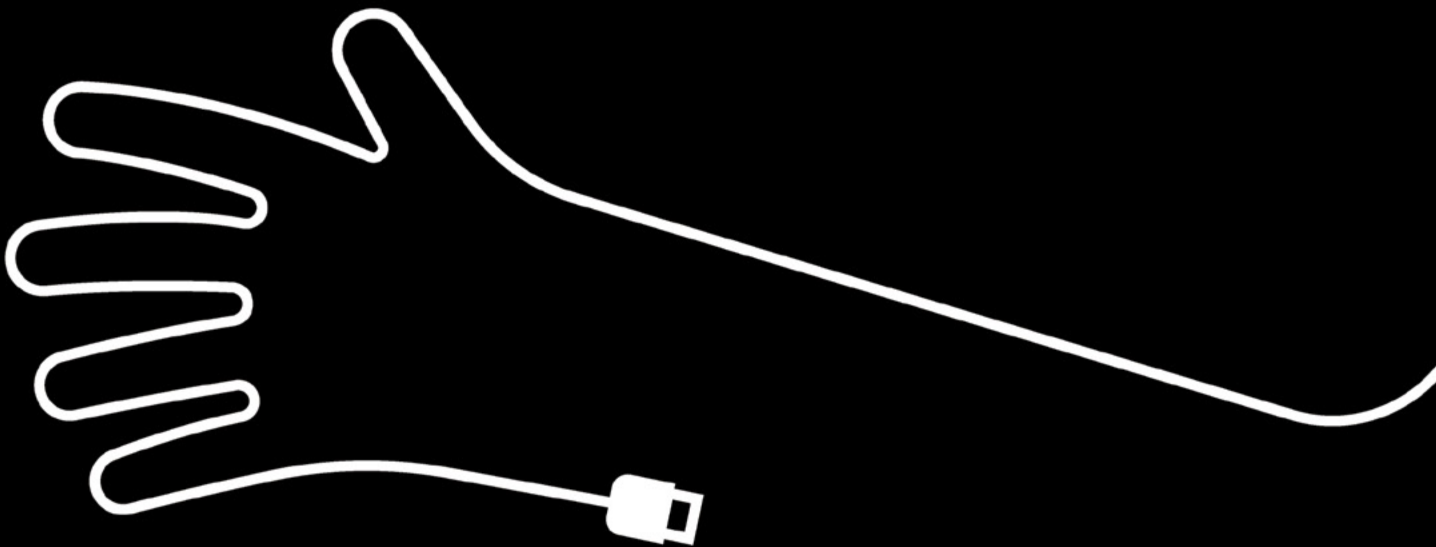


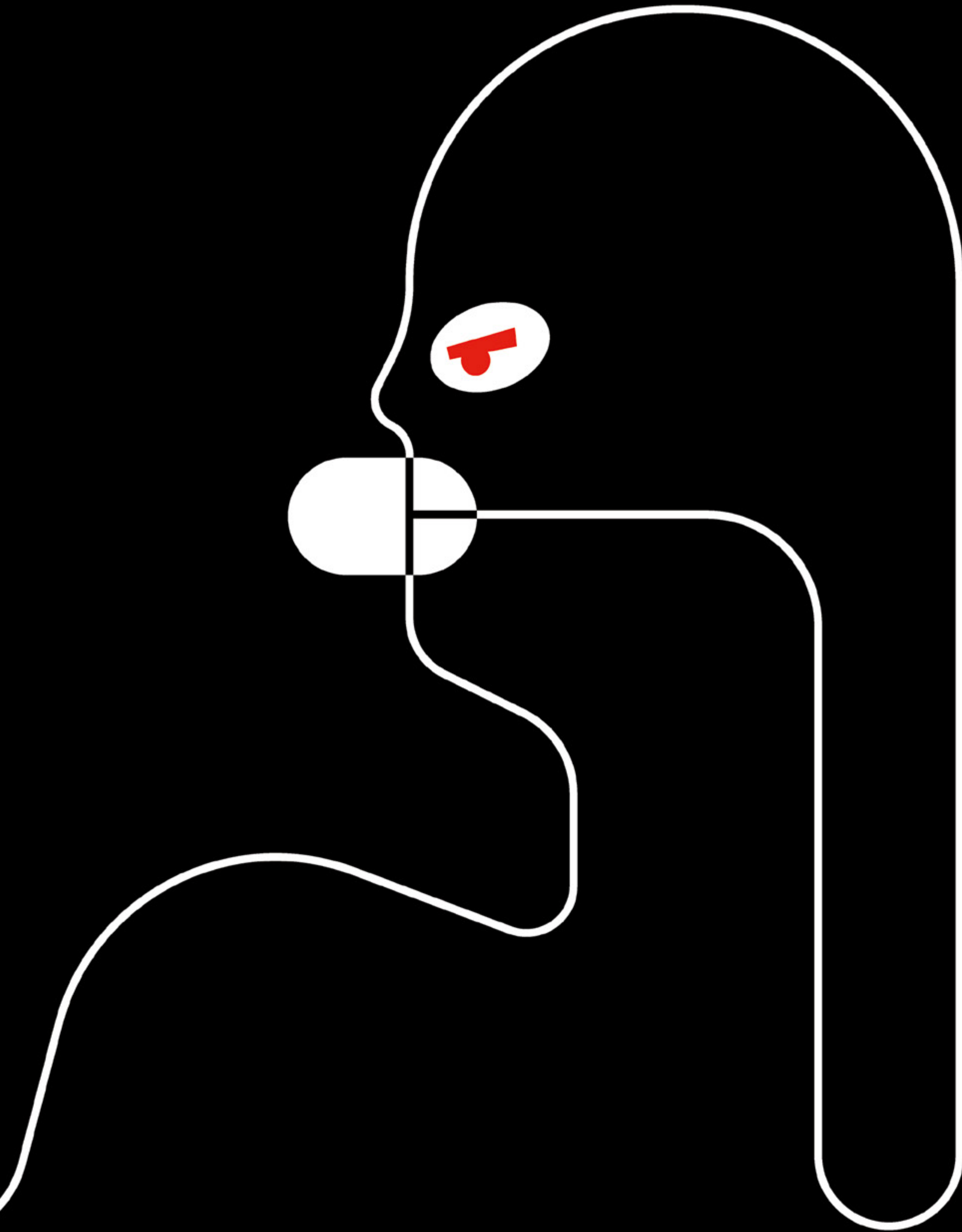
Fine art

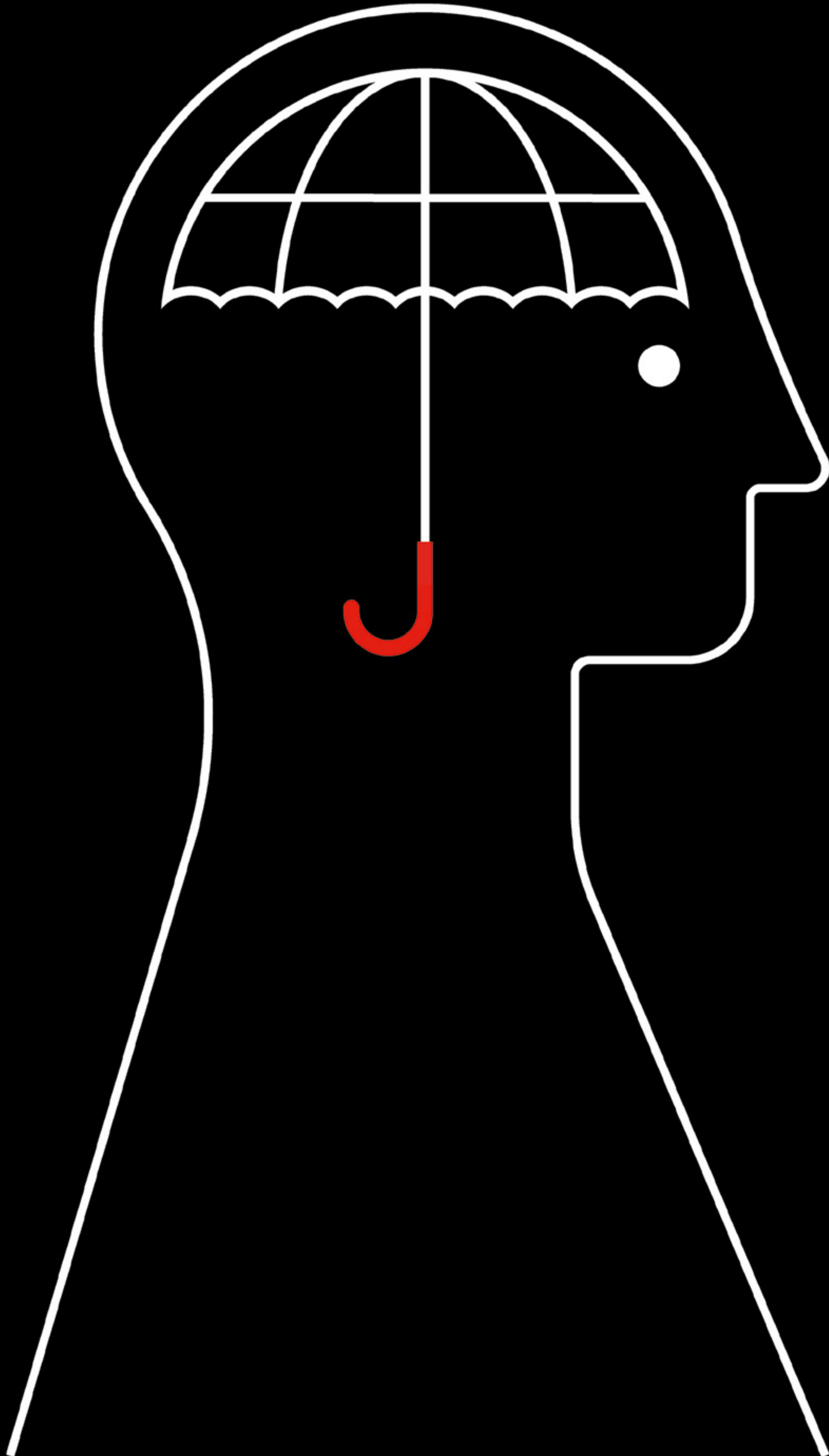
For several decades, our understanding of art has gone beyond writing policies: we promote it, we invest in it and we display it in our offices. By maintaining such an intimate knowledge of this ever-evolving and highly-specialised marketplace, and developing the skills and relationships required to successfully navigate it, we are able to offer clients the protection they demand for their artworks, every one of which is as unique as the people who create or collect them. Hiscox works closely with galleries, auction houses and museums around the world, as well as major private collectors, but we also understand that an enthusiasm for art is not restricted to large institutions and wealthy investors. So, while the majority of this business is transacted through brokers, we have also developed a simple direct-to-consumer offering to allow individuals to insure smaller collections effortlessly online.

Cyber

The market for cyber insurance is still a relatively immature one, complicated by the fast-moving nature of the threat, but as the world becomes more connected, it is also a rapidly expanding line of business. The risks associated with cyber attacks are multiplying in both diversity and scale, and the financial and reputational consequences of failing to prepare for them can be catastrophic. As a result, Hiscox – which has been underwriting cyber insurance for 20 years and now has over 80 cyber experts across the Group – has shifted the focus of its coverage from recovery to prevention, a step that demands a genuine depth of expertise. Our CyberClear products are currently sold to businesses of all sizes – from individual entrepreneurs to multinationals – through our European, US, London Market and reinsurance operations, as well as direct-to-consumers through our UK and German retail businesses. In the past year, we have dealt with over 1,000 cyber-related claims, a number which is only going to grow.







Flood
The disparate effects of climate change around the globe are an increasingly fundamental concern for the insurance industry. Because so many of the risks we underwrite are impacted by climate variability, Hiscox is investing heavily in supporting internal and external research on climate, weather and catastrophe patterns, and seeking to identify new products and services that will support customers in adapting to these far-reaching changes. Major weather events are occurring with increased frequency and severity, one of the most widespread and destructive effects of which is flooding. It's an area in which Hiscox is increasingly active. We are participants in the UK's Flood Re scheme; we have award-winning US FloodPlus products, which use proprietary technology and advanced analytics to provide more substantial cover at a fairer price than that available through the under-pressure government-backed scheme; and our reinsurance product, FloodXtra, provides a new flood insurance solution for US admitted personal lines writers. Combined, we believe these products offer the potential for significant growth in the coming years.

Small business
Across the world's most developed economies, the landscape of enterprise is undergoing a dramatic shift. Where once it was large corporations that powered economies, small businesses are now providing more of the fuel. As the digital revolution opens new avenues, the nature of small businesses – and therefore the risks they are exposed to – is also changing. At Hiscox, we have a long track record of helping entrepreneurs manage their risks, insuring around 480,000 small businesses, professionals and consultants worldwide. We understand that any small business in any sector will have its own unique character and needs. We also know that many of tomorrow's large businesses are starting out today as small ones – Hiscox itself, which began life as a partnership, is proof enough of that.

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Governance

We are a Bermuda-incorporated company and therefore not subject to the UK Companies Act and related UK secondary legislation. As a company listed on the London Stock Exchange we comply with the reporting requirements set out in the UK Corporate Governance Code (2016), and the Listing Rules and Disclosure & Transparency Rules of the UK Listing Authority (the UK's securities regulator).

In our 2016 Annual Report, our remuneration reporting was consistent with UK regulations and the policy and remuneration report were presented for an advisory vote at the Annual General Meeting on 18 May 2017 on that basis. Our remuneration reporting continues to be made on that basis.

To the extent that we have included additional disclosures over and above these requirements, it is because we believe that doing so enhances our reporting for the benefit of our shareholders, but it is done so on a voluntary basis.

Risk management

Our core business is to take risk where it is adequately rewarded, guided by a strategy that aims to maximise return on equity within a defined risk appetite.

The Group's success depends on how well we understand and manage our exposures across key risk types. These consist of strategic risk, insurance (underwriting and reserve) risk, market risk, credit risk, operational risk and regulatory, legal and tax risks. Our collective risk knowledge informs every important decision we make.

Risk strategy

Our robust risk strategy positions us to capture the upside of the risks we pursue and effectively manage the downside of the risks to which we are exposed. Our risk strategy is based upon three key principles:

- we maintain underwriting discipline;
- we seek balance and diversity through the underwriting cycle;
- we are transparent in our approach to risk, which allows us to continually improve awareness and hone our response.

Risk management framework

The Group takes an enterprise-wide approach to managing risk. The risk management framework provides a controlled system for how risk is identified, measured, managed, monitored and reported across the Group. It supports innovative and disciplined underwriting across many different classes of insurance by guiding our appetite and tolerance for risk.

Exposures are monitored and evaluated both within the business units and at Group level to assess the overall level of risk being taken and risk mitigation approaches. We consider how different exposures and risk types interact, and whether they may result in correlations, concentrations or dependencies. The overall objective is to optimise risk-return decision-making while managing total exposure in order for it to remain within the parameters set by the Board.

Risk management framework

Our continuing success depends on how well we understand and manage the significant exposures we face.

The risk management framework is underpinned by the system of internal control, which provides a proportionate and consistent system for designing, implementing, operating and assessing the internal controls that manage our key risks. The risk management framework is regularly reviewed and enhanced to reflect evolving practice on risk management and governance. During 2018, we continued the refresh of our system of internal control.

Risk appetite

Risk appetite sets out the nature and degree of risk the Group is prepared to take to meet its strategic objectives and business plan. It forms the basis of our exposure management and is monitored throughout the year.

Our risk appetite is set out in terms of risk appetite statements, which outline the level of risk we are willing to assume by risk type and overall, risk limits and tolerances, which act as boundaries where actual risk exposure is more actively monitored. Risk tolerance is the maximum threshold we do not want to exceed; nearing it would represent a 'red alert' for senior management and the Board.

Risk appetite, which is set for each of our insurance carriers and for the Group as a whole, is reviewed annually. It is flexed to respond to internal and external factors such as the growth or shrinkage of an area of the business, or changes in the underwriting cycle which may have an impact on capacity and rates.

Risk management across the business

The Group coordinates risk management roles and responsibilities across three lines of defence. These are set out in the table to the right.

Three lines of defence model

1

First line of defence
Owns risk and controls
The first line of defence is responsible for ownership and management of risks on a day-to-day basis, and consists of everyone at every level in the organisation, as all have responsibility for risk management at an operational level.

2

Second line of defence
Assesses, challenges and advises on risk objectively
The second line of defence provides independent oversight, challenge and support to the first line of defence. Functions in the second line of defence include the Group risk team and the compliance team.

3

Third line of defence
Provides independent assurance of risk control
The third line of defence is made up of the internal audit function, which provides independent assurance to the Board that risk control is being managed in line with approved policies, appetite, frameworks and processes. It also helps verify that the system of internal control is effective.

Risk is also overseen and managed by formal and informal committees and working groups across the first and second lines of defence. These focus on specific risks such as catastrophe, reserving, investments and credit, as well as emerging risks. The Group Risk and Capital Committee and the Group Underwriting Review Committee make wider decisions on risk.

The role of the Board in risk management

The Board is at the heart of risk governance and is responsible for setting the Group's risk strategy and appetite, and for overseeing risk management (including the risk management framework).

The Risk Committee of the Board advises on how best to manage the Group's risk profile by reviewing the effectiveness of risk management activities and monitoring the Group's risk exposures, to inform Board decisions. The Risk Committee relies on frequent updates from within the business and from independent risk experts.

During 2018, the Board and Risk Committee reviewed a number of risk-related matters.

- The Group's risk profile, compared with its Board-approved risk appetite.
- Independent second line of defence model validation findings on the Group's capital model.
- Risk reporting focused on topical live issues with actions and mitigation plans.
- Regular reporting on the risks determined by the Board to be critical to the Group.
- Stress and scenario testing, performed to identify and measure the likelihood and impact of potentially plausible, but extreme, events. This included consideration and challenge of the findings and associated action plans for the scenarios, which had been designed to test the resilience of the business plan to major and minor shocks.
- Updates to the risk and control register, which summarises the Group's material risk exposures and the key controls in place to mitigate them, as agreed with risk owners.
- Updates to Group risk policies, addressing the Group's main risks.
- The Group Solvency Self-Assessment (GSSA) report, which builds on many of the components described above to summarise the Group's Own Risk and Solvency Assessment (ORSA), which is described further in the following section.

This year, topics have included the direct and indirect implications of geopolitical and macroeconomic forces, such as Brexit, changes to governments, the impact of shifting trade relations and volatility in financial markets.

Strategic risk

ORSA process

Hiscox's ORSA process is an evolution of its long-standing risk management and capital assessment processes. It is the self-assessment of the risk mitigation and capital resources necessary to achieve the strategic objectives of the Group and relevant insurance carriers on a current and forward-looking basis, while remaining solvent, given their risk profiles.

Role of the Group risk team

The Group risk team is responsible for designing and overseeing the implementation of the risk management framework and continually improving it. The team works with the business units to understand how they manage the risks in the first line and whether they need to make changes in their approach. The team is also responsible for monitoring that the business meets regulatory expectations around enterprise risk management and reporting on risk to the Board and the Risk Committee.

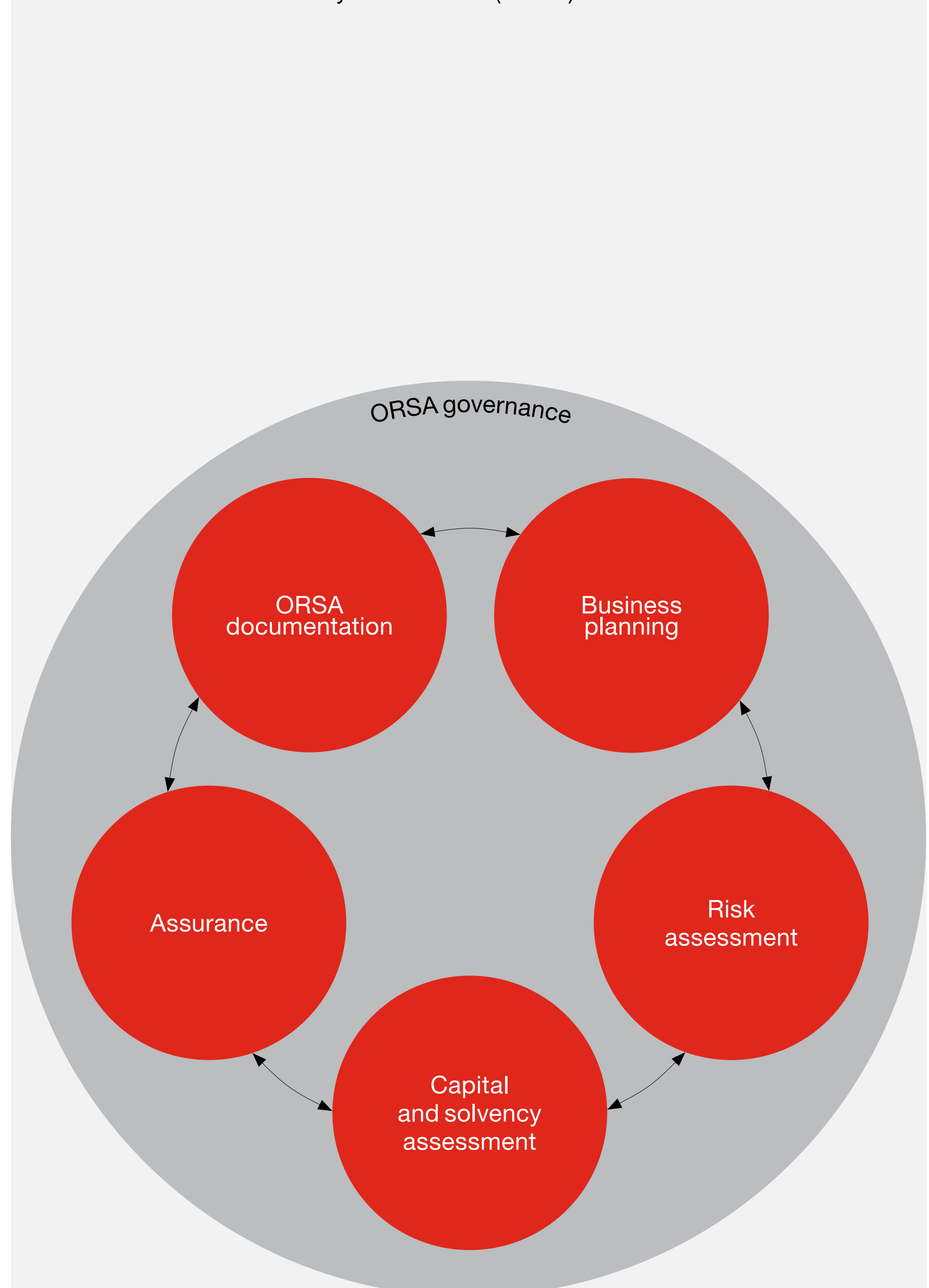
The Group risk team is led by the Chief Risk Officer, who reports to the Chief Executive and the Chair of the Hiscox Ltd Board Risk Committee.

2017 and 2018 have seen the recruitment and on-boarding of business unit risk managers who provide risk management advice on the ground, further enhancing the breadth and capability of the second line.

Principal risks

The principal risks facing the organisation are described on the following pages.

Hiscox Own Risk and Solvency Assessment (ORSA) framework



Strategic risk

The possibility of adverse outcomes that may result from strategic 'bets'/business initiatives taken or not taken by the Group. This may include business expansion or contraction, mergers and acquisitions, negative impact to reputation or brand, or failure of the Board to provide adequate oversight of the business or make appropriate business decisions.

What is the risk?	Why do we have it?	How is it managed?
Strategy evolution and execution The Group's continuing success depends on: i) how well we understand our clients, markets and the various internal and external factors affecting our business; and ii) having a strategy in place to address risks and opportunities arising out of this. Not having the right strategy could have a detrimental impact on profitability, capital position, market share and reputation.	Setting the right course and long-term strategic objectives at a high level is essential for the long-term success of the Group. This is especially important because some strategic initiatives require multi-year commitment and execution.	A key strategic principle for the evolution of Hiscox is to balance the underwriting of high-margin, volatile, complex global risks with comparatively stable, local specialist retail products. Each of the businesses pursues its strategic objectives as set out by the business unit leadership teams and approved by the relevant Board through the operating plan process. In addition, the Executive Committee sets out a common set of strategic objectives for the Group that cut across businesses and functions. These are based on the collective understanding of internal challenges and priorities, as well as external factors. Furthermore, the Group's emerging risk forum assesses risks and opportunities that could potentially affect the business. This year, topics have included the direct and indirect implications of geopolitical and macroeconomic forces, such as Brexit, changes to governments, the impact of shifting trade relations and volatility in financial markets. Additional consideration has been placed on items that have already emerged but are constantly evolving, assessing the secondary impact of these on our business and the markets in which we operate. Consideration was also given to the impact of various post-Brexit scenarios, with their impact on strategy and performance of the business being assessed as part of business planning. We have taken measures to ensure that the solution we have put in place in response to Brexit is appropriate regardless of the final outcome of government negotiations. Stress testing and scenario analysis help identify possible dependencies and correlations between risks, which could impact on the Group's strategy.

Insurance risk – underwriting

The risk that insurance premiums will not be sufficient to cover future insurance claims and associated expenses. It also encompasses people, process and system risks directly related to underwriting, such as human error in paying invalid claims or misquoting premium prices.

What is the risk?	Why do we have it?	How is it managed?
Pricing This is the risk of failing to price policies adequately, or making poor risk selection decisions. Hiscox competes against major international insurance and reinsurance groups. At times, competitors may choose to underwrite risk at prices below the break-even technical price. Prolonged periods in which premium levels are low or competition is intense are likely to have a negative impact on the Group's financial performance. Accepting risks below their technical price is detrimental to the industry. It can drive market rates down to a point where underwriting losses mount, insurers' capital is reduced and some businesses fail. Customers could receive poor service and the industry could suffer negative publicity.	We operate in open, aggressively competitive markets in which barriers to entry for new players are relatively low. Competitors may choose to differentiate themselves by undercutting their rivals. As a result, capacity levels in these markets rise and fall, causing prices to go up and down, creating volatile market cycles.	We adapt our desire to write certain lines of business according to market conditions and the Group's overall risk appetite. We reject business unlikely to generate underwriting profits and regularly monitor pricing levels, producing detailed monthly reports on how pricing and exposures are developing. This allows us to quickly identify and control any problems created by deteriorating market conditions. Hiscox frequently acts as the lead insurer in the co-insurance programmes needed to cover high-value assets, so we have some ability to set market rates. Delegated authorities give the Group access to a greater volume of business and can contribute significantly to our profitability and market share. The Group rewards its staff for producing profit not revenue. This helps to maintain underwriting discipline in soft markets. Pricing policies have been developed for each legal entity and class of business. In addition, some classes of business maintain more detailed technical underwriting guidelines. Pricing adequacy is assessed via the peer review process. All underwriters and classes of business are subject to peer review. All underwriters and classes of business are also subject to independent review. In addition, the Group Chief Underwriting Officer commissions a series of independent portfolio reviews, including file reviews, providing a formal critique of the underwriting approach and strategy for classes of business or products that are typically either new, unproven or have recently missed budget.

Insurance risk – underwriting continued

What is the risk?	Why do we have it?	How is it managed?
Underwriting exposure management Hiscox insures individual customers, businesses and other insurers for damage caused by a range of catastrophes, both natural (for example, hurricanes or earthquakes) and man-made (for example, terrorism), which can cause heavy underwriting losses that materially impact the Group's earnings and financial condition if they occur. The Group buys reinsurance protection to manage catastrophe risk and reduce the volatility that major losses could have on our financial position. If the Group's reinsurance protection were proven to be inadequate or inappropriate, it could significantly affect our financial condition.	Underwriting large, volatile and complex risks can be potentially costly, but can also create strong returns over the medium to long term. The scope and type of protection we buy may change from year to year depending on the extent and competitiveness of cover available in the market.	The Group underwrites catastrophe risk in a carefully managed, controlled manner. Our strategy of creating and maintaining a diversified portfolio, both by product and geography, helps limit our overall catastrophe exposure. The Group's business plan is underpinned by a clearly-defined appetite for underwriting risk. We closely monitor our risk exposure to maximise the expected risk-return profile of our entire portfolio and offset any potential losses from more volatile accounts. Peer review assesses whether or not risks are in line with underwriting appetite. Underwriters are incentivised to make sound decisions that are aligned with the Group's strategic objectives and risk appetite, and clear limits are placed on their underwriting authority. In response to legal developments, policy wordings are regularly reviewed to ensure that, as far as possible, exposure to those risks identified in the policy at the time of issue is maintained. Our modelling resources are tailored to support insurance and reinsurance plans and ensure that exposure matches expectations. Risk aggregation and modelling resources are shared across the Group. Comprehensive stress and scenario testing is performed to assess our potential exposure to certain catastrophes. We buy reinsurance to reduce our risk exposure and mitigate the impact of catastrophes based on a clear outwards reinsurance strategy and centralised reinsurance programme that enables us to minimise gaps in coverage across the business and get the right deal by leveraging our size. Decisions about the type and amount of reinsurance we buy are supervised by a dedicated reinsurance purchasing team using modelling techniques. Oversight is provided by a number of key committees, including the reinsurance purchase group.
Authority breach This is the risk of accepting underwriting risks outside of agreed underwriting parameters or where authority limits have been breached. Hiscox assigns underwriting parameters based on a number of factors, including level of experience and skill of the individual. These parameters are in place for all relevant Hiscox employees and those that fall under a third-party delegated authority.	Accepting risks outside of agreed underwriting appetite, regardless of source, can result in unplanned or misunderstood underwriting exposures.	Underwriter authority letters (UALs) are in place for all underwriters and reviewed at least annually. The underwriting control function maintains records of the UALs. Potential breaches of UALs are monitored periodically and escalated where necessary to senior management. Material underwriting breaches are reported to the nominated Director and relevant division management team. Peer reviews and technical underwriting reviews assess whether or not UALs are adhered to. With respect to parties with delegated underwriting authority, authorities granted by Hiscox are closely controlled through strict underwriting guidelines, contractual restrictions and obligations. A Group-wide delegated authority policy sets out clear standards and principles for managing the delegation of authority to external third parties. We vet all third parties prior to appointment and monitor and audit them regularly.

Insurance risk – reserving

The risk of unsuitable case reserves (for example, over- or under-reserving) and/or insufficient technical reserves in place to meet incurred losses and associated expenses.

What is the risk?	Why do we have it?	How is it managed?
Reserve risk The Group makes financial provisions for unpaid claims, defence costs and related expenses to cover liabilities both from reported claims and from 'incurred but not reported' (IBNR) claims. If insufficient reserves were put aside to cover our exposures, this could affect the Group's future earnings and capital.	When underwriting risks, we estimate both the likelihood of claims occurring and their cost. Our actual claims experience could exceed our expectations, requiring us to increase our levels of reserves held.	The provisions we make to pay claims reflect our own experience and the industry's view of similar business. They are also influenced by loss payments, pending levels of unpaid claims, historic trends in reserving patterns and potential changes in rates arising from market or economic conditions. Provisions are set above the actuarial best estimate to reduce the risk that actual claims may exceed the amount we have set aside. Our provision estimates are subject to rigorous controls and review by all areas of the business, as well as by independent actuaries. The relevant boards approve the amount of the final provision, on the recommendation of dedicated reserving committees. Details of the actuarial and statistical methods and assumptions used to calculate reserves are set out in note 23 to the consolidated financial statements.

Credit risk

The risk of loss or adverse financial impact due to default by counterparties to which Hiscox is exposed.

What is the risk?	Why do we have it?	How is it managed?
Credit risk – reinsurance The Group buys reinsurance to protect us, but if our reinsurers were unable to meet their obligations to us it could put a strain on our earnings and capital, and harm our financial condition and cash flows.	We cover clients against a range of catastrophes and protect ourselves through reinsurance. We face credit risk when we seek to recover sums from our reinsurers.	We buy reinsurance only from companies we believe to be strong. A dedicated Reinsurance Credit Committee, a subcommittee of the Group Credit Committee, must approve the use of every reinsurer, based on an assessment of their financial strength, trading record, payment history, outlook, organisational structure and external credit ratings. Our credit exposures to these companies are closely monitored, as are the companies themselves, so we can quickly identify any potential problems. We consider public information, our experience of the companies, their behaviour in the marketplace and consultants' and rating agencies' analysis.
Credit risk – brokers If a broker defaults, causing them to fail to pass premiums to us or fail to pass the claims payment on to a policyholder, this can result in us losing money.	A significant portion of our business is written through brokers. We face credit risk when money is transferred to and from brokers for premiums or claims.	We monitor our exposure to brokers on an ongoing basis and have continued dialogue with our core brokers to quickly identify and resolve any credit issues that arise. Such monitoring takes into account a number of factors, which can include credit rating, financial position, financial performance, payment history and market factors. In the case of some large losses, we pay policyholders directly to reduce broker credit risk on material transactions.

Market risk

The threat of unfavourable or unexpected movements in the value of Hiscox's assets and/or the income expected from them.

What is the risk?	Why do we have it?	How is it managed?
Asset value Money received from our clients in premiums, and the capital on our balance sheet, is invested until it is needed to pay claims or other liabilities. These funds can be exposed to investment risk. Investment risk also includes the risk of default of investment counterparties, who are primarily the issuers of bonds in which we invest.	The investment of the Group's assets generates an investment return. Our investment portfolio is exposed to a number of risks including, but not limited to, changes in interest rates, credit spreads and equity prices.	Our objective is to maximise risk-adjusted investment returns in the prevailing financial, economic and market conditions, without creating undue risk to the Group's capacity to underwrite. Funds held for reserves are invested primarily in high-quality bonds and cash. To reduce foreign exchange risk, these are usually maintained in the currency of the original premiums for which they were set aside. As many of our insurance and reinsurance liabilities have short time spans, we do not aim to match exactly the duration of our assets and liabilities. The Group's fixed-income fund managers operate within clear guidelines as to the type and nature of bonds in which they can invest. These prioritise the need to pay claims while providing sufficient flexibility to enhance returns. A proportion of funds is allocated to riskier assets, principally equities and hedge funds. By taking a long-term view on these assets, we seek to achieve the best possible risk-adjusted returns. Within our risk assets, we make an allocation to less volatile, absolute return strategies, which balance our desire to maximise returns with the need to ensure capital is available to support our underwriting throughout any downturn in financial markets.
Liquidity A failure of our liquidity strategy could leave us unable to meet cash requirements to pay liabilities to customers or other creditors when they fall due. We might also incur high costs in selling assets or raising money quickly in order to meet our obligations. Such a failure could have a material adverse effect on the Group's financial condition and cash flows.	If a catastrophe occurs, the Group may be faced with large, unplanned cash demands. This could be exacerbated by having to fund a large number of claims pending recovery from our reinsurers. Although our investment policies stress the conservation of principal and liquidity, our investments are subject to market-wide risks and fluctuations.	The Group's investment policy recognises the demands created by our underwriting strategy, so that some investments may need to be sold before maturity or at short notice. A high proportion of our investments are in liquid assets, which reduces the risk of losses being incurred if a quick sale is needed. Funds held for reserves are invested primarily in high-quality, short duration bonds and cash so the Group can meet its aim of paying valid claims quickly. The Group's cash requirements can normally be met through regular income streams: premiums, investment income, existing cash balances or by realising investments that have reached maturity. Our primary source of inflows is insurance premiums, while our outflows are largely expenses and payments to policyholders through claims. We forecast our cash flow for the week, month, quarter, or up to three years ahead, depending on the source. To identify potential issues, we run stress tests to estimate the impact of a major catastrophe on our cash position. We also consider the impact on our liquidity of other adverse events occurring, such as an economic downturn and declining investment returns. The Group maintains extensive borrowing facilities with a range of major international banks. This minimises the risk of one or more institutions being unable to honour commitments to us.

Operational risk

The risk of direct or indirect loss resulting from internal processes, people or systems, or external events.

What is the risk?	Why do we have it?	How is it managed?
Information security (including cyber security) A failure to properly protect information could compromise the confidentiality, integrity or availability of our information and data. Cyber security risk is a subset of information security risk and is the threat to the Group posed by the higher maturity of attack tools and methods, the increased exposure and the increased motivation of attackers. As well as causing financial losses, information and cyber security risks can have legal, regulatory and reputational consequences.	Our business is based on trust from customers and partners, and that trust depends on our ability to keep their information secure. We operate in a world in which the volume of sensitive data and the number of connected devices and applications have increased exponentially, while cyber attacks are increasingly frequent and sophisticated. Our business depends on the confidentiality, integrity and timely availability of the information and data we maintain, own and use.	The information security group, which is chaired by the Chief Financial Officer and attended by the information security risk owners, manages the risk in line with the Group's risk appetite, supported by experts from around the business. The Group employs dedicated information security resources to advise on information security design and standards, and conduct assurance activities. Our defensive capabilities include industry standard monitoring with additional protection for specific, highly confidential information. The Group invests in a rolling programme that deploys and evolves systems, policies and procedures to mitigate internal and external threats to our IT infrastructure. We conduct Group-wide mandatory training on information and cyber security, which is also mandatory for all third parties and contractors. Our stress testing and scenario analysis considers the impact and likelihood of information security exposures and assesses management actions, including response plans.
Information technology and systems failure A major IT, systems or service failure could have a significant impact on our business.	Our information technology and systems are critical to conducting business and providing continuity of service to our clients, including supporting underwriting and claims processes.	We have dedicated IT resources that support the Group's technology needs and oversee critical systems and applications. Our stress testing and scenario analysis considers the impact and likelihood of an IT or systems failure and assesses how management actions could be taken to mitigate the risk. A formal disaster recovery plan is in place to deal with workspace recovery and the retrieval of communications, IT systems and data should a major incident occur. These procedures would enable us to quickly move the affected operations to alternative facilities. The plan is tested regularly and includes simulation tests.
Project risk and change management This is the risk that projects and/or change initiatives are not delivered to plan, budget or specification, or that the risks inherent in projects, or the interdependencies across projects, are not appropriately managed. Where this occurs, there may be not only direct financial losses, but also indirect losses through distraction risks and inefficiencies.	We operate in an ever-changing environment, with technological advancements, customer behaviour and external expectations evolving rapidly in recent years. To remain relevant, we must continue to evolve how we conduct our business.	All major programmes have dedicated project governance structures to oversee their delivery of the programme, including risk management aspects. Programme sponsors also provide updates to the Boards and Risk Committees as appropriate. Heads of change in business units and for the Group provide portfolio-level oversight of risks, issues and resource needs across projects. This includes the evolution of project governance and the coordination of best practice guidance. The programme assurance office is a second line function that provides oversight across all major programmes. It provides senior management with an independent view of the progress, risks and issues within the programmes, as well as the linkages between them. Specialist resource is used to augment project resources, either in a contractor or advisory capacity, as needed.

Regulatory, legal and tax risks

The risk of financial loss, regulatory censure, additional taxation, reputational damage and/or other adverse impact as a result of non-compliance with all relevant regulatory, legislation and tax requirements in all relevant jurisdictions.

What is the risk?	Why do we have it?	How is it managed?
Regulatory, legal and tax change The insurance industry is exposed to continuous regulatory, legal and tax change. There is a risk that we fail to act in accordance with relevant regulatory requirements in all relevant jurisdictions or that there is deterioration in the quality of our relationship with one or more of our regulators.	We operate in a global environment and insurance is a highly-regulated financial industry. There may be times when the regulatory, legal or tax landscapes undergo significant change that directly impacts our business. For example, local country tax authorities are evolving their approach and expectations with regards to the transparency and nature of the tax base.	The Group understands that sound, prudent regulation is key to the stability and sustainability of the insurance market and wider financial markets. We continuously monitor new regulation and review our internal processes to facilitate compliance. Our approach is to combine local expertise with a globally consistent framework to manage regulatory, legal and tax change and provide effective compliance with the various and evolving requirements.

Responsibility

Our values underpin a reputation we have earned for integrity and decency in everything we do. We understand we are part of something beyond our bottom line and we take our role in the world seriously.

Being good to our environment

Hiscox is committed to reducing the environmental impact of its work. Our environmental policy sets out the standards we aim to achieve throughout the Hiscox Group by minimising our direct emissions, and actively seeking to identify new products and services that support our customers in adapting to the effects of climate change.

We aim to complete a 15% real-term reduction in our Scope 1, 2 and 3 carbon emissions per full-time equivalent (FTE) by 2020, relative to 2014, and are already ahead of target. The table on page 53, which depicts the Group's global carbon emissions year-on-year since 2015, shows that travel is currently the biggest contributor. We will commence work on our new targets for beyond 2020 in 2019.

We also remain fully committed to being a carbon neutral business. We choose to offset our global emissions through a carbon offset scheme which is reviewed annually. In 2018, we worked with Carbon Footprint Ltd in the Great Rift Valley in Kenya for the second consecutive year. This scheme uses carbon finance to fund tree planting and support the local community, and offsets our 9,197 tonnes of carbon emissions.

Hiscox is a founding member of ClimateWise, a global network of more than 20 leading insurance companies which aims to leverage insurers' collective expertise to better understand, communicate and act on the risks associated with climate change. We also work closely with Lloyd's and the Association of British Insurers (ABI) on these issues. Since the network's launch in 2008, our progress in meeting a set of principles outlined by ClimateWise has been subject to annual independent review. In 2018, we were given a score of 74%, our highest score from ClimateWise to date, ranking us eighth among the participants. A full copy of the Hiscox Climate Report is available at www.hiscoxgroup.com/responsibility.

Hiscox is a constituent of indexes including CDP and the FTSE4Good Index, a series of benchmark and tradable indices designed to help investors integrate environmental, social and governance (ESG) factors into their investment decisions.

We are also exploring how we can align our approach to climate change, and to manage our environmental impacts to the UN Sustainable Development Goals, which are increasingly seen as the international standard for businesses to more consistently and collaboratively engage with the sustainable development agenda.

Being a good corporate citizen

As a business

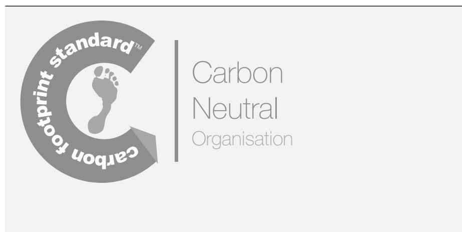
We hold ourselves to high standards of professionalism and ethical practice in every part of our business and operate in accordance with our values, which are outlined on page 7. Our belief is that insurance is a promise to pay: should a loss occur, we aim to support our customers and pay every valid claim as quickly as possible.

We adapt the products we sell as traditional risks evolve and new risks emerge – both climate-related and otherwise. More information on how we manage our underwriting exposure to risks including natural catastrophes can be found in the risk management section on pages 42 to 51. In particular, we have done a lot of work recently around flood risk in the UK and USA. Through our participation in the UK's Flood Re scheme and our US FloodPlus and FloodXtra products, we are now protecting more homeowners at risk of flooding who otherwise would have had no cover or not enough cover. We are also piloting schemes such as Leakbot, which monitors water pressure and can alert a homeowner through an app if there is a drop in pressure (an early-warning indicator of a possible leak).

Hiscox UK & Ireland and Hiscox London Market both have the Chartered Insurance Institute's Chartered Insurer status, and we consider this an important marker for attracting high-quality business partners such as brokers. The risks we write through brokers account for approximately 90% of our business, so it is essential that we build strong and lasting relationships with those brokers that share our values. It is why we have instigated a 'superb service' ethos, designed to develop a greater understanding of brokers' needs, and is also why we run annual broker summit events for our senior broker partners and for the rising stars in their businesses.

Our suppliers are also important to us. They enable us to function to the highest standards and put customers back together again swiftly when the worst happens, so we expect all our suppliers to reflect our values and adhere to the same high standards as we do in order to provide the kind of customer service that our reputation is built upon.

At the heart of our business is claims. In 2018, we paid out a total of $1.2 billion in claims worldwide, helping to get individuals and businesses back on their feet after the worst happened. This is exactly what we are here for. When we get this right, a by-product is the good feedback we get from our customers and the awards we receive, which are listed on page 6.



Global emissions

	2015	2016	2017	2018
Scope 1 – company car use, on-site gas combustion and refrigerant loss	590	612	742	750
Scope 2 – purchased electricity	2,113	2,175	1,889	1,582
Total (scope 1 and 2)	2,703	2,787	2,631	2,332
Tonnes CO_2e per FTE (Scope 1 and 2)	1.20	1.14	0.97	0.76
Scope 3 – air, rail and personal car business travel	4,538	4,596	5,151	6,865
Total (all scopes 1, 2 and 3)	7,241	7,383	7,782	9,197
Tonnes CO_2e per FTE (all scopes 1, 2 and 3)	3.22	3.02	2.88	2.98

We are only human though, and sometimes we get it wrong. When this happens, and our customers are not as satisfied as we would want, we do our best to remedy this.

We also communicate openly and transparently with our shareholders, reporting both our half-year and full-year results to investors via a series of presentations, and sharing all relevant financial information on the corporate website, www.hiscoxgroup.com. Executives meet regularly with investors and analysts to discuss the Group's strategy and performance and to answer any questions. More information on shareholder engagement can be found in the corporate governance section on pages 61 to 64.

Conduct

Treating our customers fairly and helping them to achieve the best possible outcome is central to the Hiscox culture. We aim to ensure that high standards of customer service are adhered to across the customer journey for consumers and corporates alike. Excellent customer experience is an important pillar of management decision-making and our corporate philosophy. It is good for our customers, but also helps us meet regulatory expectations and protects the hard-earned value of our brand.

Identification of conduct risk (the risk of our actions leading to poor outcomes for customers) is an operational and strategic imperative. We seek out customer feedback and learn from qualitative and quantitative analysis of customer interactions to improve the design of products, sales, service and claims processes. A culture and process of continuous improvement helps us to meet our customers' expectations, manage risk and continue to succeed.

Attracting and retaining good people

We employ over 3,300 people across 14 countries and in some cities, such as York in the UK, we are a major local employer. No matter where they are based, we require all our staff to behave according to the core values of the Group. By doing so, we believe we are more likely to achieve business success, create value for shareholders, and attract and retain staff.

There are many ways in which we seek to attract talent.

- We have two graduate schemes: one for underwriters, and a commercial programme for areas of specialism such as marketing, IT or HR. Each scheme gives individuals the opportunity to undertake a series of rotations, working in different parts of our business, and to gain comprehensive training through professional qualifications. Our graduate programme has evolved over the years, but since the scheme began in 2009 we have taken on over 150 graduates from a wide variety of universities. The scheme continues to play a major role in our youth attraction strategy, with graduates past and present helping us to refine and improve the programme year after year.
- We also have a three-year actuarial training programme which builds on the skills and technical knowledge gained from university for those thinking of a career as an actuary. The programme combines in-house courses with specialist external training, and on-the-job experience across different actuarial functions including pricing and capital management. It also offers the possibility of an overseas placement to one of our offices in the USA, Bermuda or Europe.
- Specifically in the UK, we offer a small number of places on our three-and-a-half-year degree-qualified apprenticeship scheme. The scheme provides those who have not gone to university or college with the opportunity to complete a degree at the same time as gaining valuable business experience, and is available for a wide variety of roles – from underwriting and claims to operations, marketing and finance.
- We offer a small number of paid summer internships each year across our UK, US and European businesses, which equip students with real-life workplace skills. Some of our interns have even made their way back to Hiscox after graduation.

When it comes to retaining talent, we aim to provide all of our staff with both the means and the motivation to succeed in their career at Hiscox, and recognise that different things motivate different people.

- We encourage employees to share in the Group's success through competitive pay, profit and performance-related bonuses, Save As You Earn (SAYE) schemes, executive performance share plans, and a contributory pension scheme. Salary packages are benchmarked against the financial services industry as a whole and against the Lloyd's market specifically (where applicable), and are also considered on a country-by-country basis. These benefits are appealing to our employees and in 2018, 73% of employees paid into one of our SAYE schemes.

- We provide opportunities for our staff to work flexibly to suit their personal circumstances. These include revised start or finish times, remote working or reduced days. In 2018, we received 113 formal flexible working requests from employees across the Group, 93% of which were approved in full.
- We promote health and well-being by providing private medical cover, bi-annual health checks and subsidised health club membership.
- We are committed to training and development and all employees have access to a range of resources to help in their career development, both internally and externally. Success Factory is our internal training tool and contains hundreds of different courses covering technical and professional development, honing leadership skills and how to have more productive performance review meetings. In 2018, over 31,000 training hours were completed through Success Factory and many more hours of external training, coaching and mentoring were delivered. This figure also excludes all mandatory training undertaken around areas including

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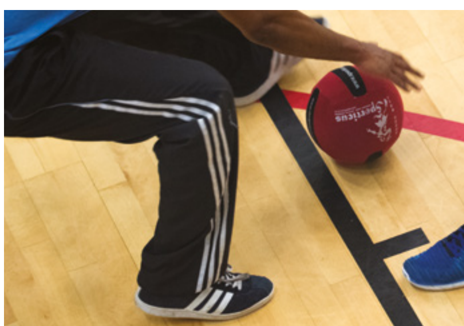
Attracting and retaining good people



cyber and the new EU General Data Protection Regulation (GDPR). We operate in a highly-regulated industry and take our responsibilities in this regard seriously. For example, as part of our induction process in the UK, individuals are required to complete six regulatory assignments within three months of joining: Hiscox conduct risk and treating customers fairly; Hiscox introduction to the FCA; Hiscox money laundering and how you can prevent it; what whistleblowing is and why we need it; Hiscox data protection training; and business ethics. This training ensures a consistent level of understanding across the business to matters including anti-bribery and anti-corruption as well as other important business ethics issues. We also support those pursuing professional qualifications on the job, such as AAT for our accounting teams or ACII for our underwriters. Training and development needs are formally reviewed twice a year as part of our Group-wide performance management and review process, which is also when performance is measured against clearly-set objectives.

Employee engagement
We listen to the views of our people and encourage them to contribute to the progress of the business by sharing feedback and new ideas. Employees are kept informed of business developments through formal briefings, town hall events, team meetings, intranet bulletins, video conferences and other more informal routes, and we work hard to ensure this is a two-way dialogue. For example, once employees have settled into their job at Hiscox, staff at all levels of the business are invited to lunch with members of the Executive Committee, to share their ideas for improvement and innovation and views on Hiscox as a place to work.

Policies
We have a range of policies in place that guide our business, some of which are set out below.

Diversity and inclusion policy
We want to build teams that are as diverse as the customers and communities we serve and create an environment where all our people can thrive. Our diversity and inclusion policy, and the culture and processes we are embedding in our business, help us to do this. More information on our progress in diversity and inclusion can be found on page 56.

Environmental policy
Our environmental policy outlines our approach to managing the environmental impact of our business activities and those that arise from our ownership and occupation of office premises. We actively manage and aim to minimise our environmental impacts, due to the resources we consume and the amount of waste our activities produce, as well as complying with relevant environmental legislation and other requirements such as the ClimateWise Principles.

Equality policy statement
Our equality policy statement outlines our aim to provide equal opportunities to all in employment, irrespective of gender, race, disability, age, sexuality, religion, beliefs, marital status and social class. Hiscox strongly opposes all forms of unlawful and unfair discrimination.

Financial crime policy and framework
We updated our financial crime policy this year. It provides consistent standards and guidelines for the Group and sets out our position in relation to matters including sanctions, counter-terrorist financing, anti-money laundering, anti-bribery and corruption, fraud and anti-facilitation of tax evasion. It reflects the values of our business, one of which is integrity, and our commitment to honest and fair dealing in all activities. Preserving our culture of transparency and accountability at the same time as ensuring compliance with applicable financial crime laws and regulations is important to us, and we will not tolerate breaches of these rules. The revised financial crime policy and framework consolidates and supersedes a number of previous policies for the Group.

Health and safety policy
Our health and safety policy is to provide a work environment and work activities that ensure the health, safety and welfare of all our employees and those who are affected by our operations across all Hiscox Group activities and locations.

Modern slavery statement
Hiscox complies with the provisions of the Modern Slavery Act. Our modern slavery statement outlines our zero-tolerance approach to slavery or human trafficking in our supply chains or in any part of our business.

Respect for human rights
Maintaining a positive, open and inclusive culture that respects our colleagues' human rights is fundamental to the Group's strategy. We do not maintain a stand-alone human rights policy, but are guided by the principles of the UN's Universal Declaration of Human Rights and the International Labour Organisation's core labour standards.

Whistleblowing policy
Our whistleblowing policy, which we updated in 2018, ensures employees feel empowered to raise concerns relating to malpractice or wrongdoing in confidence and without fear of unfair treatment. If an employee has a serious concern relating to the operation of the business, our whistleblowing procedures enable them to confidentially raise their concerns with senior management or, if they choose, with the Chair of the Hiscox Ltd Audit Committee. All Hiscox staff can also access free, confidential advice from the whistleblowing charity Public Concern at Work.

We also conduct an annual global employee engagement survey, a formal mechanism for checking how our staff are thinking and feeling and which gives us the ability to benchmark against the wider financial services industry. In our 2018 employee engagement survey 86% of staff say they are proud to work for us, 94% said they believe in our corporate values and 80% said they would recommend Hiscox as a great place to work. Each year the survey results are shared throughout our business via emails, intranet articles and presentations from business leaders where our people also have the opportunity to discuss the results and question the actions that will be taken. Business units each review what is said for their area, and many establish representative working groups to drive the employee agenda and help make tangible, practical changes. This has included creating new communications channels, such as monthly newsletters, in those parts of the business that have said they want more frequent communications from senior leaders.

We strive to remain, in essence, a non-bureaucratic organisation. We have an effective system of internal controls to ensure that risks are managed within acceptable limits, which are outlined in the risk management section on pages 42 to 51, but these do not come at the expense of innovation or speed of response. Our ability to strike this balance, while achieving the highest standards of corporate governance as detailed on pages 61 to 64, is one of the Group's greatest strengths.

Giving back to our community

The Group is fully committed to supporting the communities within which it operates, through donations, professional support and the volunteer work of its employees. In 2018, our teams around the world contributed to the following charitable endeavours.

Diversity and inclusion (D&I)

D&I remained a Group-wide priority in 2018 and we made good progress here.

The interest in employee networks that we saw in 2017 is bearing fruit, with new employee networks focused on parents, mental health and well-being, generations, the pan-African and Latino communities and LGBT proving popular. Over 740 employees have already signed up as employee network members and over 25 events have taken place, including talks on topics such as managing stress, insuring women's futures, and navigating difficult conversations. These networks not only provide people with a forum for focused discussion, they have also led to practical initiatives such as lunchtime 'walk and talk' events in our London office and well-being lunches in our art cafés. We are especially pleased that, in our three largest UK offices, we have established a network of mental health first-aiders. These trained individuals are publicised throughout each building in the same way as physical first-aiders, and are on-hand to support colleagues with their mental health and well-being and direct them to expert resources as required.

This year we piloted unconscious bias training for all people managers in the USA and all employees in Germany. Through our partnership with PDT, a global D&I training consultancy, we have trained over 110 employees this year, with roll-out across the Group in 2019 ensuring that everyone managing a team will be trained within the next 12-18 months. This training is important in uncovering employees' own personal biases and learning how to challenge them, and we will continue its roll-out to other parts of our business.

The women in leadership training we launched in 2015 has now been completed by 175 female employees and continues to prove popular. Based on 2015-2017 analysis, 86% of employees felt the training was beneficial and have been able to apply it to a real-world work situation, and 34% have since been promoted. We have extended the course to more junior employees this year and will continue to roll-out this training in 2019.

For the fourth consecutive year, we supported the Dive In Festival – an annual series of events around D&I that takes place across 26 countries and 50 cities. Our teams attended a number of these events, and our Group Head of Claims Supplier Management, Andrew Sellers, delivered a keynote address on creating an open, empowering and inclusive workplace.

A new area of focus this year has been supporting women in their return to work after maternity leave. New handbooks that improve clarity around what to expect from work before, during and after your new arrival have been developed to help employees and managers, and a buddy system has been introduced which matches new parents returning to work with others who can share their experience and offer advice and support.

We also took important steps towards improving our recruitment efforts by using diversity job boards, partnering with more diverse schools and universities and making D&I part of the discussion with external recruiters and hiring leaders. We aim to have diverse interview panels and diverse candidate slates for jobs across the Group, and ensure that job descriptions are gender neutral.

The second of our gender pay reports was published at the end of the year. It showed a small year-on-year improvement in our median pay gap, though the pay gap between men and women remains higher than we would like at 24.5% (2017: 26.2%). This is still mainly driven by the fact that we have more men than women in more senior, higher-paid roles and we continue to work hard to address this – with D&I remaining a strategic priority for the Executive Committee in 2019.

- 2018 saw the official launch of our Hiscox Gives charity initiative, which supports charities chosen by employees and aims to raise awareness and encourage volunteering across the Group. Our London office chose to support three local charities – KEEN London, Providence Row and The Felix Project – through a combination of fundraising and volunteering. London staff have responded well to a renewed focus on volunteering, with over 70 people signed up to take part, and over 390 hours of volunteering completed. Other initiatives such as the reading partners scheme, which involves working with children in local primary schools, through to the Lloyd's Community Programme, continue.
- Hiscox London Market commenced a multi-year partnership with the Dust Project, a charity which helps disadvantaged children in Sri Lanka by pairing building projects with child sponsorship. In 2018, the first year of our support, we raised over £11,000, and eight of our London Market team went to Sri Lanka to help build the first house for a disadvantaged family. The team were so moved by their trip that they now also sponsor eight local children through their education. We will continue to support the charity and its goal of building 20 houses in the next five years through 2019 and beyond.
- Community work was also undertaken across many of our other UK offices. In Colchester, staff raised over £13,000 for their chosen cause, Cohoc, the Colchester Hospitals charity, through fundraising efforts including running the Colchester Half Marathon and abseiling down their local town hall. This money has enabled Cohoc to purchase a new incubator to help care for sick or premature babies. In York, the team raised over £11,000 for York SANDS (Stillbirth and Neonatal Death Society), which saw employees bungee jumping from the Middlesbrough Transporter Bridge. The team also continued to cultivate the colony of bees that we have installed on the roof of our office, and supported the Yorkshire Air Ambulance as part of a multi-year partnership.
- Hiscox Bermuda supported organisations working with local young people, the elderly and the most vulnerable members of the community. These groups included The Family Centre, The Duke of Edinburgh Award Programme, The Bermuda Housing Trust, The Bermuda Education Network, Meals on Wheels and Habitat Bermuda. We also continued our sponsorship of the Caines Brothers Back2School event by providing 350 backpacks and lunch boxes so that all children, no matter their circumstances, could return to school well-equipped for the new school year. We maintained our support for various environmental groups including Greenrock, Keep Bermuda Beautiful and Friends of the Bermuda Railway Trail and this year supported the Bermuda Zoological Society's Kids on the Reef programme. We provided scholarship opportunities for Bermuda students through donations to the Association of Bermuda International Companies and the Alpha Phi Alpha Beautillion. We continue to sponsor the Bermuda Cricket Board's under 11 cricket league and the ever-popular Hiscox Cricket Festival.
- Hiscox USA supported charities local to its offices that focus on education, medical science, advancement of the arts and culture or provision of services to disadvantaged and vulnerable communities.
- Hiscox Iberia continued to participate in the annual 1kg of Help campaign, working with brokers and other business partners to donate food to those in need during the festive season.
- Hiscox Benelux supported two new charities this year with donations to help those diagnosed with cancer and Alzheimer's disease.

For more detail on corporate responsibility see **hiscoxgroup.com**

The Hiscox Foundation supported a number of these efforts. The Foundation is funded by an annual contribution from the Group, which makes grants to social and humanitarian initiatives and contributes to the fundraising activities of Hiscox employees. In total, the Hiscox Foundation in the UK and USA donated over $480,000 during 2018.

The Group is also a passionate supporter of the arts, science and technology. In the UK, Hiscox supported the City of London's Sculpture in the City project for the eighth consecutive year, and continued to be the insurance partner of the Whitechapel Gallery, a free-to-access gallery close to our London office that champions contemporary art. We are The National Gallery's first Contemporary Art Partner, and this multi-year partnership continued in 2018, as did our support of Art Night – a free contemporary arts festival that puts art into extraordinary locations around London for one night a year, encouraging the public to experience art and their city through fresh eyes. Through ArtUK, we support the Masterpieces in Schools programme, which enables schools in the UK to apply to have a sculpture visit their school and helps make art more accessible to more people. This year, we also commenced a three-year partnership as corporate supporters of The Hepworth Wakefield. Hiscox Germany continued to support promising young artists, presenting a €7,500 prize to the best young artist selected by a jury at Hamburg's renowned university of fine art, HFBK, and supporting another artist with an artist-in-residence scholarship. Meanwhile, Hiscox France worked with FIAC, France's premier art fair.

Hiscox was title sponsor of The Sunday Times Hiscox Tech Track 100 for the sixth consecutive year. It charts the fastest-growing private technology, telecoms and digital media companies in the UK, many of which we are proud to support as customers.

Board of Directors

Robert Simon Childs
Non Executive Chairman (Aged 67)
*26 February 2013**

Robert Childs joined Hiscox in 1986, served as the Active Underwriter of the Hiscox Lloyd's Syndicate 33 between 1993 and 2005, and was the Group's Chief Underwriting Officer until February 2013, when he became Non Executive Chairman. In 2012, Robert joined the Council of Lloyd's and in 2017 became Deputy Chairman of Lloyd's.

Hamayou Akbar Hussain
Chief Financial Officer (Aged 46)
*12 September 2016**

Aki Hussain joined Hiscox in 2016 from Prudential plc, where he spent seven years; latterly as Chief Financial Officer of Prudential UK and Europe. Prior to his time with Prudential, Aki held a number of senior roles in the financial services, telecoms and media sectors. He was Finance Director for the consumer bank division at Lloyds Banking Group until 2009, before which he was Finance Director for the consumer division of ntl (now Virgin Media). Aki is a Chartered Accountant, having trained with KPMG.

Bronislaw Edmund Masojada
Chief Executive (Aged 57)
*11 October 2006**

Bronek Masojada joined Hiscox in 1993 as Group Managing Director and he became Chief Executive in 2000. From 1989 to 1993 he was employed by McKinsey & Company. Bronek served as Deputy Chairman of Lloyd's from 2001 to 2007 and was Chairman of the Lloyd's Tercentenary Research Foundation from 2008 to 2014. He is currently a member of the Board of the Association of British Insurers and a Director of Pool Reinsurance Company Limited. In March 2018 he took over as Chair of Placing Platform Limited, the organisation responsible for moving the London insurance market to an electronic trading platform.

Richard Colin Watson
Chief Underwriting Officer (Aged 55)
*16 May 2013**

Richard Watson joined Hiscox in 1986, having previously worked for Sedgwick and Hogg Robinson. In 2005, he was appointed Managing Director of Hiscox Global Markets, the largest division of Hiscox by premium income, and was the Underwriter of Syndicate 33 from 2006 to 2009. In 2009, Richard moved to New York and served as the Chief Executive Officer of Hiscox USA for three years. He returned to London in 2012 and became Chief Underwriting Officer for the Hiscox Group.

Lynn Pike
Independent Non Executive Director (Aged 62)
*20 May 2015**

Lynn Pike joined Hiscox in May 2015. Lynn has 38 years' experience in the banking industry, most recently as President of Capital One Bank. Prior to joining Capital One, Lynn was President of Bank of America's small business banking division, a $2.1 billion revenue business, with oversight of 110,000 business clients and 2,000 employees. Dividing her time between California and Connecticut, Lynn currently serves on the private Board of American Express National Bank, California State University Channel Islands Foundation Board, Phoenix House Foundation, and on Bankwork$' Advisory Board.

Caroline Foulger
Independent Non Executive Director (Aged 58)
*1 January 2013**

Caroline Foulger joined Hiscox in January 2013 having retired from a partnership at PwC. Until May 2012, Caroline led PwC's insurance and reinsurance practice in Bermuda. Caroline is a Fellow of the Institute of Chartered Accountants in England and Wales, a member of the Institute of Chartered Accountants of Bermuda and a member of the Institute of Directors. Caroline is a Non Executive Director of the Bank of N.T. Butterfield & Son Limited and Oakley Capital Investments Limited.

Hiscox Ltd

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△ Member of the Audit Committee
□ Member of the Remuneration Committee
⬡ Member of the Nominations and Governance Committee

▲■⬢
Chairman of Committee is highlighted in solid.

*Effective date of Hiscox Ltd contract.

△□⬡

Michael Goodwin
Independent Non Executive Director (Aged 60)
*16 November 2017**

Michael Goodwin joined Hiscox in November 2017. He has over 25 years' experience in the insurance industry having worked for QBE Insurance between 1992 and 2012. He held a number of roles for QBE in the Australian and Asia Pacific markets and was Chief Executive Officer of QBE Asia Pacific from 2007 to 2012. Michael is a Fellow of the Institute of Actuaries of Australia.

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Thomas Hürlimann
Independent Non Executive Director (Aged 55)
*16 November 2017**

Thomas Hürlimann joined Hiscox in November 2017. Thomas has 29 years' experience in banking, reinsurance and insurance, most recently as CEO Global Corporate at Zurich Insurance Group, a business with $9 billion premiums and a network in over 200 countries. Before that he worked at Swiss Re and started his career with National Westminster Bank. Thomas is also a Non Executive Director of WiseKey and a Senior Advisor to Drake Star Partners. He holds an MBA from IMD.

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Colin Keogh
Independent Non Executive Director (Aged 65)
*19 November 2015**

Colin Keogh joined Hiscox in November 2015. Colin has spent his career in financial services, principally at Close Brothers Group plc, where he worked for 24 years and was Chief Executive Officer from 2002 until 2009. He is a Non Executive Director of M&G Group Limited and Chairman of specialist financial services business Premium Credit Limited.

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Anne MacDonald
Independent Non Executive Director (Aged 63)
*20 May 2015**

Anne MacDonald joined Hiscox in May 2015. Anne has held the position of Chief Marketing Officer at four different Fortune 100 companies, marketing some of the most recognisable corporate names in the world – from Citigroup and Travelers to Macy's and PepsiCo. With an MBA from Bath University, Anne is currently a Director of New York Stock Exchange-listed company Boot Barn. She was formerly a Director of NASDAQ-listed Rentrak Corporation, stepping down from the Board on completion of its merger with comScore, Inc.

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Robert McMillan
Independent Non Executive Director (Aged 66)
*18 November 2010**

Bob McMillan joined the Hiscox Ltd Board in December 2010. He spent 24 years with the Progressive Insurance Corporation, where he served in various positions including National Director of Product Development, then claims, before becoming National Director of Marketing. He led Progressive's initiatives in multi-channel distribution, financial responsibility-based rating, and immediate response claims. He has received two United States patents related to motor insurance pricing. He has lectured at the University of Virginia's Darden School of Business and at the Harvard Business School. He has been a Non Executive Director of Hiscox Inc. since March 2007.

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Constantinos Miranthis
Independent Non Executive Director (Aged 55)
*16 November 2017**

Costas Miranthis joined Hiscox in November 2017. He was President and CEO of PartnerRe, a position from which he stepped down in 2015. Prior to joining PartnerRe in 2002 he was a Principal of Tillinghast-Towers Perrin in its London office with responsibility for the European non-life practice. He is a Fellow of the Institute and Faculty of Actuaries and a member of the American Academy of Actuaries. He is also a past Chair of the European Reinsurance Association Board.

Chairman's letter to shareholders
Key developments on corporate governance throughout the year.

Dear Shareholder
The robust governance framework which underpins our business model continues to evolve in line with our operations and as our business grows. For Hiscox, good governance is much more than compliance with codes, and we work hard to ensure we have the right culture, a balanced Board with diversity among our independent Non Executives and a well-defined network of committees.

The arrangements we have in place in relation to governance are described in detail within our corporate governance section on pages 61 to 64, but I would like to highlight a few notable events since last year's report.

- The Financial Reporting Council published a revised UK Corporate Governance Code (the 2018 Code), which applies to accounting periods from 1 January 2019. We have carefully reviewed the Code to ensure that our governance practices not only reflect the requirements but also the spirit of the Code. Where necessary we have updated our Terms of Reference for the Committees to better reflect their responsibilities and will report our compliance with the 2018 Code in next year's Report and Accounts.
- The Companies (Miscellaneous Reporting) Regulations 2018 came into force. The regulations came into effect for financial years beginning on, or after, 1 January 2019 and introduce a number of new reporting requirements for quoted companies incorporated in the UK including: disclosures regarding the way companies engage with their employees; enhanced reporting on governance arrangements; a requirement to disclose Chief Executive pay ratios; and how directors fulfil their statutory duties. Although the new regulations do not apply to Hiscox as a Bermuda incorporated company, we believe in maintaining the highest standards of disclosure and transparency, and accordingly we will include additional disclosures in our 2019 Report and Accounts where we think to do so would improve our narrative reporting and give shareholders a better understanding of our corporate governance arrangements. In that spirit, we have decided to voluntarily report our Chief Executive's pay ratio, which is included in our annual report on remuneration on pages 72 to 83.
- As part of the continued evolution of our risk management approach, Group risk owners across our business completed the Risk and Control Self-Attestation process – a formal declaration of adherence to over 40 principles.
- In the UK the Senior Managers and Certification Regime (SMCR) replaced the Senior Insurance Managers Regime (SIMR) this year. The regime aims to reinforce the importance of individual accountability, especially at senior levels, but also to encourage personal responsibility at all levels. Work with Board members and the Executive Committee was undertaken in 2018 to ensure our compliance with SMCR, and we will continue to evolve this process in 2019 when certification will be required from additional members of the organisation.
- The Nominations and Governance Committee has assumed responsibility for the review of potential conflicts, therefore a specific Conflicts Committee is no longer required.
- An externally facilitated evaluation of the Board was conducted to follow up on the external evaluation carried out in 2017. It considered progress made against the issues highlighted in last year's evaluation and included a review of Board composition; whether there was an appropriate balance of skills, experience, independence and knowledge; and whether the Board worked together as a unit. The key outcomes from the latest evaluation are summarised on page 63.

Robert Childs
Chairman

Corporate governance

As the size and shape of the Hiscox Group continues to grow and develop it is vital that we have in place a robust governance framework which underpins our business model.

Overview and basis of reporting

Hiscox Ltd (the Company) is the Bermuda incorporated holding company for the Group and has a premium listing on the London Stock Exchange. The corporate governance framework for the Company is derived from its constitution together with the Bermuda Companies Act. The Listing Rules require the Company to report against the UK Corporate Governance Code published in April 2016 (the Code). During 2018, and up to the date of this Annual Report and Accounts, the Group has complied with the provisions of the Code in all material respects. The Financial Reporting Council (FRC) published a revised UK Corporate Governance Code (the 2018 Code) in July 2018 which applies to accounting periods beginning on, or after, 1 January 2019. The Company intends to report against this version in next year's Report and Accounts.

The Board of Directors

As at the date of this report, the Board comprises the Non Executive Chairman, three Executive Directors, and eight independent Non Executive Directors including a Senior Independent Director. Biographical details for each member of the Board are provided on pages 58 to 59. The roles and activities of the Chairman and Chief Executive are distinct and separate. The Chairman is responsible for running an effective Board including oversight of corporate governance and strategy. The Chief Executive has responsibility for running the Group's business.

The Nominations and Governance Committee (formerly the Nominations Committee) monitors the composition of the Board and considers its diversity, balance of skills, experience, independence and knowledge to ensure that it remains appropriate. The Committee is also responsible for monitoring developments relating to corporate governance and informing the Board accordingly. The composition of the Board was reviewed as part of the Board evaluation described on page 63.

Non Executive Directors are subject to annual appointment. Their terms of appointment state that their continuation in office is contingent upon their satisfactory performance and prescribe the time commitment required of them in order to discharge their duties. The terms of appointment also state that appropriate preparation time is required ahead of each meeting. The remuneration of the Non Executive Directors does not include performance-related elements and is reviewed periodically.

The Board has set voluntary restrictions on the number of other Directorships a Non Executive Director is permitted to hold. The external commitments of the Chairman and the Executive Directors are disclosed in their profiles on page 58.

While the Board acknowledges the value that knowledge and experience of the organisation can bring, it also recognises the need to progressively refresh Board membership over time. Non Executive Directors will normally be expected to serve for six years. They may be invited to serve for longer, but service beyond nine years is unlikely. Any service beyond six years is subject to a particularly rigorous review. Bob McMillan was appointed to the Board in 2010 and, in accordance with the criteria set out in the Code, potentially ceases to be independent if he continues to serve beyond nine years. Accordingly, Bob McMillan will not seek re-appointment at the 2019 Annual General Meeting and will retire from the Board.

In accordance with the Company's Bye-Laws, all Directors, with the exception of Bob McMillan, will seek re-appointment at the 2019 Annual General Meeting.

The Chairman, Robert Childs, did not meet the independence criteria set out in the Code on appointment. Nevertheless, the Chairman acts in an independent manner, and the Board is satisfied that the Chairman performs an independent function, and continues to demonstrate objective independent judgement. The Board also believes that the Chairman's experience and expertise in underwriting and risk management is a valuable asset in the performance of its functions, including the oversight of the Group's risk strategy and appetite and risk management framework. The Board considers all other Non Executive Directors to be independent within the meaning of the Code as there are no relationships or circumstances which would interfere with the exercise of their independent judgement.

All Directors have access to the Company Secretary for advice and guidance on matters relating to corporate governance, and they are all entitled to seek independent professional advice at the Company's expense. As part of the Board evaluation conducted during the year, Directors were asked to assess the quality of the support they receive from the Company Secretary and the support was rated highly. The Board meets at least four times a year in person with scheduled calls in between. In addition, the Board operates within established Terms of Reference and receives appropriate and timely information to enable Directors to review business strategy, trading performance, business risks and opportunities.

During the year, Directors received briefings on areas including Hiscox marketing initiatives, major transformation programmes, regulatory updates and data strategy.

The Board of Directors

The Board held four scheduled meetings during 2018.

There is a formal induction process for new Directors. The needs of a new Director joining the Board are assessed and appropriate training arranged. No new Directors joined the Board in 2018. Directors' training requirements were assessed as part of the Board evaluation process and existing Directors were provided with the opportunity to attend training sessions. During the year, Directors received briefings on areas including Hiscox marketing initiatives, major transformation programmes, regulatory updates and data strategy, as well as in-focus sessions on specific business units and business unit initiatives.

The Board's Terms of Reference include a Schedule of Matters Reserved for Board Decision, a copy of which can be found on the Group's website, www.hiscoxgroup.com. Aside from the opportunity that Non Executive Directors have to challenge and contribute to the development of strategy in regular Board meetings, Non Executive Directors also attended the annual Hiscox Partners' meeting held during the year.

The Board retains ultimate authority for high-level strategic and management decisions such as setting Group strategy and Group investment strategy, as well as approving matters including: significant mergers or acquisitions; the Group financial statements, declaration of interim dividends and recommending the final dividend; Group business plans and budgets; major new areas of business; capital raising; bonus issues or rights issues of share capital; Directors' remuneration; significant expenditure or projects; and the issue of share awards.

The Board has appointed an Executive Committee and authorised the boards of the trading entities and business divisions to manage their respective operational affairs, to the extent that Board or Executive Committee approval is not required.

The Board's committees

The Board has appointed and authorised a number of committees to manage aspects of the Group's affairs, including financial reporting, internal control and risk management. Each committee operates within established written Terms of Reference and each committee Chairman reports directly to the Board.

The Board and Committee meetings usually take place over two days when all of the Directors convene in Bermuda. Prior to the Board and Committee meetings taking place, the Board and the Executive Committee together hold in-focus sessions exploring specific aspects of the Hiscox Group. These presentations are sometimes made by members of the Executive Committee, or other members of the management team, or in some cases by individuals with particular expertise in certain markets.

The Audit Committee

The Audit Committee of Hiscox Ltd comprises Caroline Foulger, Michael Goodwin, Thomas Hürlimann, Colin Keogh, Anne MacDonald, Bob McMillan, Costas Miranthis and Lynn Pike. Caroline Foulger is considered by the Board to have recent and relevant financial experience and is Chair of the Committee. The Audit Committee as a whole is considered to have competence relevant to the sector in which the Company operates. Further information on the background and experience of the Committee members is included in their profiles on pages 58 and 59. The Audit Committee operates according to the Terms of Reference published on the Group's website and met four times during the year to assist the Board on matters of financial reporting and internal control, and to determine the external auditor's fees. The Committee monitors the scope, results and cost effectiveness of the internal and external audits, the independence and objectivity of the external auditor, and the nature and extent of non-audit work undertaken by the external auditor together with the level of related fees. The Audit Committee receives reports from the external auditor who also attend meetings of the Committee to report on the status of their audit and any findings. This allows the Committee to monitor the effectiveness of the external auditor during the year.

PwC was appointed as the Company's external auditor at the 2016 Annual General Meeting. There are currently no plans to re-tender the audit. The internal and external auditors have unrestricted access to the Committee. All non-audit work undertaken by the Group's external auditor with fees greater than £50,000 must be approved in advance by the Committee. PwC has confirmed to the Committee that in its opinion it remains independent and the Committee is satisfied that this is the case. In respect of the 2018 financial year, the Committee reported to the Board on how it had discharged its responsibilities, provided advice to the Board on how the Annual Report and Accounts were fair, balanced and understandable, and provided the information necessary for shareholders to assess the Company's position and performance, business model and strategy. Further information on the activities of the Committee is included in the Audit Committee report on pages 65 and 66. The arrangements by which staff may, in confidence, raise concerns about potential improprieties are described in the responsibility section on pages 52 to 57. The arrangements were reviewed, updated and reissued to all employees across the Group in July 2018.

The Remuneration Committee

The Remuneration Committee comprises, Caroline Foulger, Michael Goodwin, Thomas Hürlimann, Colin Keogh, Anne MacDonald, Bob McMillan, Costas Miranthis and Lynn Pike. It is chaired by Colin Keogh and met four times during the year. The Remuneration Committee takes care to recognise and manage conflicts of interest when receiving views from Executive Directors or senior management, or consulting the Chief Executive about its proposals. No Executive is permitted to be present when the Committee discusses his or her remuneration. The Committee's role in remuneration is described in the remuneration section on page 69. The overall aim is to attract and retain high-calibre individuals and incentivise them to deliver long-term success for the Company. Executive Directors are subject to malus and clawback provisions in relation to their remuneration and the circumstances in which these would apply are described on page 90.

The Nominations and Governance Committee

The Nominations and Governance Committee comprises Robert Childs, Caroline Foulger, Michael Goodwin, Thomas Hürlimann, Colin Keogh, Anne MacDonald, Bob McMillan, Costas Miranthis and Lynn Pike, and is chaired by Robert Childs. The Committee's role is to monitor the structure, size and composition of the Hiscox Ltd Board and, when Board vacancies arise, to nominate, for approval by the Board, appropriate candidates to fill those roles. The Group believes that opportunity should be limited only by an individual's ability and drive, and the Committee considers diversity – including gender diversity – when recommending appointments to the Board. For example, the Committee has a policy in place to ensure that the candidate pool for each new appointment includes at least one female but does not consider it appropriate to set quotas for diversity. More information on the Group's diversity policies and work during the year can be found in the responsibility section on pages 52 to 57.

The Nominations and Governance Committee has a role in considering the succession planning for Executive Directors and senior managers, and a remit to make recommendations on the succession planning for the Chairman and the Chief Executive and other members of the senior management group.

The Nominations and Governance Committee is also responsible for reviewing the Company's compliance with the Code, making any recommendation regarding changes to the Company's corporate governance. During the year, the Committee received a briefing on the 2018 Code.

The Nominations and Governance Committee has assumed responsibility for the review of potential conflicts, therefore a specific Conflicts Committee is no longer required.

The Investment Committee

The Investment Committee has oversight of the Group's investments and comprises Robert Childs, Caroline Foulger, Michael Goodwin, Thomas Hürlimann, Colin Keogh, Anne MacDonald, Bob McMillan, Costas Miranthis, Lynn Pike, the Chief Executive and the Chief Financial Officer and is chaired by Robert Childs. At each meeting the Committee receives an update from the Chief Investment Officer on the performance of the Company's and the Group's investment portfolios. The Investment Committee normally meets four times a year.

The Risk Committee

The Risk Committee oversees the risk management framework and advises the Board on how best to manage the Group's risk profile. The Committee comprises Robert Childs, Caroline Foulger, Michael Goodwin, Thomas Hürlimann, Colin Keogh, Anne MacDonald, Bob McMillan, Costas Miranthis and Lynn Pike. It is chaired by Lynn Pike and normally meets four times a year. The risk management framework is described in the risk management section on pages 42 to 51.

The Group has a dedicated risk team led by the Chief Risk Officer, which reports to both the Risk Committee of the main Board and to those of the relevant subsidiary Boards. At each of its meetings during the year the Risk Committee reviews and discusses a risk dashboard and a critical risk tracker which monitors the most significant exposures to the business, including emerging risks and risks that have emerged but are evolving. The Risk Committee also engages in focused reviews, with recent topics being data security and the potential impact of climate change. Stress tests and reverse stress tests (scenarios which could potentially give rise to business failure as a result of a lack of viability or capital depletion) are also performed and reported on to the Risk Committee. In light of these arrangements the Directors are satisfied that a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity, has been carried out during the year.

The Executive Committee

The Executive Committee comprises Senior Executives and normally meets every six weeks. It makes recommendations to the Board and approves various matters. The Committee approves senior appointments and remuneration outside the scope of the Nominations and Governance Committee, approves operational policy, takes decisions on annual budgets, business plans, mergers and acquisitions, considers significant issues raised by management and approves exceptional spend within the limits established by the Board. Below this there are local management teams that drive the local businesses.

Performance evaluation

The Code requires an externally facilitated Board evaluation to be undertaken every three years and this last took place in 2017. Since the last report, a follow-up evaluation was conducted, which included a review of Board composition; whether there was an appropriate balance of skills, experience, independence and knowledge; and whether the Board worked together as a unit. It also asked Directors to rate the level of diversity of the Board. Other areas covered were succession planning, Board meeting content and focus, the support to the Board, the quality and provision of information, the Non Executive Directors' input into the strategy and shareholder engagement. The findings of the evaluation were discussed by the Board as a whole.

Overall the evaluation found that the Board's composition and dynamics were rated highly, but the value of further increasing the Board's diversity was also recognised. The testing and development of strategy was positively rated, as was the Board's monitoring of culture and its understanding of employee needs. It was noted that there was scope to further focus on succession plans for Executive Committee members, and retaining and developing talent. The other key areas of focus for the Board in response to the evaluation are a continued focus on corporate culture and values, strategy and customer feedback, greater interaction with employees, improving understanding of technological and digital developments, and closer monitoring of competitor performance, as well as a continued focus on risks.

In addition to the forward-looking evaluation of the Board, the Senior Independent Director, Colin Keogh, met with the other Non Executive Directors without the Chairman present to appraise the performance of the Chairman. During the year, the Non Executive Directors also periodically met without the Executive Directors to discuss a wide range of issues concerning the Company and the Group.

No issues arose that would prevent the Chairman from recommending the re-appointment of a Non Executive Director. The Chairman met with the Chief Executive, and the Chief Executive met with each of the Executive Directors, to discuss their performance over the year and to set targets for the year ahead.

An alert service is available on **hiscoxgroup.com** to notify any stakeholder of new stock exchange announcements.

Shareholder engagement

Shareholder engagement

Directors communicate and meet directly with shareholders and analysts throughout the year, and do not limit this to the period following the release of financial results or other significant announcements. The views expressed by shareholders have been reported back to the Board through its committees and any specific items covered in letters received from major shareholders are also reported to the Board. All Directors attended the Annual General Meeting in 2018.

On a regular basis, following the Group's results announcements, Hiscox commissions independent research on feedback from shareholders and analysts. This research, together with the analysts' research notes, is shared with the Non Executive Directors in full. The Chairman attends a number of meetings with shareholders and investors.

Major shareholders are invited to request meetings with the Senior Independent Director and/or the other Non Executive Directors. An alert service is available on www.hiscoxgroup.com to notify any stakeholder of new stock exchange announcements.

Accountability and internal control

Risk is at the heart of any insurance organisation and the management of risk is fundamental to the success of its business model. The principal risks facing the organisation are described in the risk management section on pages 42 to 51 together with an explanation of how they are managed or mitigated. These risks are managed dynamically in response to changing circumstances. For example, more work has been completed this year around the risk and control self-attestation process, as noted in the Chairman's letter to shareholders on page 60.

Emerging risks often influence our strategic approach, and are considered holistically as part of the wider risk landscape. These principal risks comprise the Group's 'critical risks', or exposures which materially threaten financial strength, severely impact business operations or significantly affect strategy. Critical risks often develop over a short time, or offer limited time to react, respond or recover, thereby requiring continuous focus. The Group is subject to regulatory requirements aimed at ensuring its continuing solvency and has established arrangements to assess and manage its principal risks continually. Risk and solvency assessments are conducted and the Group is required to assess the capital resources necessary to achieve its strategic business objectives over the coming year while remaining solvent, given its risk profile. This includes a forward-looking assessment which considers the business plan over a three-year period.

Going concern and viability

Notwithstanding the uncertainties arising from the risks summarised on pages 42 to 51, there is a statement on page 94 which confirms that for the 2018 financial year the Directors considered it appropriate to adopt the going concern basis of accounting. For the reasons explained above, the prospects of the Company are assessed over a longer period than the 12 months required by the Code. The Group calculates and projects forward the capital requirements of its regulators and those of the rating agencies to ensure that it will continue to meet any applicable solvency requirements and achieve the ratings it feels are necessary to conduct its business profitably. While the Board has no reason to believe the Group's business model will not be viable over a longer period, the period over which the Board considers it possible to form reasonable expectations as to its position is the three years to 31 December 2021. This corresponds to the forward-looking element of the Group's regulatory solvency assessments and allows reliance to be placed on the output from those assessments as well as the other arrangements described above. On the basis of its robust assessment of the principal risks, and on the assumption that they can continue to be managed or mitigated as described (and taking account of the most recent solvency assessments, together with the results of the stress tests and focused risk reviews), the Board has a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to 31 December 2021.

As part of the Group's internal controls, the internal audit function provides objective and independent assurance and advice to the Audit Committee and the Board over the processes and systems of internal control and risk management operating in the Group. It achieves this through an annual risk-based programme of reviews, the scope of which considers an independent view of the risks facing the Group, as well as other factors such as strategic initiatives, emerging risks and change. It includes an annual review of the Group's compliance with the governance requirements emanating from its regulators and the Code. The findings of these internal audit reviews are reported to the Audit Committee. The Audit Committee oversees the internal control and risk management system in relation to financial reporting. Further details are set out in the Audit Committee report on pages 65 to 66.

Taken together, the risk and internal control activities described here enable the Board to monitor the Group's risk management and internal control systems. The Board has concluded that the Group's risk management and internal control systems are effective.

Audit Committee report

Financial reporting

In relation to financial reporting, the primary role of the Audit Committee (the Committee) is to monitor the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance, and review significant financial reporting judgements contained within them. Working with both management and the external auditor, the Committee reviewed the appropriateness of the half-year and annual financial statements, concentrating on, among other matters:

- the quality and acceptability of accounting policies and practices;
- the clarity of the disclosures and compliance with financial reporting standards and relevant financial and governance reporting requirements;
- material areas in which significant judgements and estimates have been applied or there has been discussion with the external auditor;
- any correspondence from third parties in relation to our financial reporting.

To aid the review, the Committee considered the key judgements and estimates found in the financial statements by the Chief Financial Officer, as well as reports from the external auditor on the outcomes of its annual audit and half-year review. The Committee supported the auditor, PwC, in displaying the necessary professional scepticism its role requires. The primary areas considered by the Committee in relation to the 2018 Annual Report and Accounts were:

i) The reserving for insurance losses

As set out in our significant accounting policies on pages 112 and 113, the reserving for insurance losses, in particular losses incurred but not reported, is the most critical estimate in the Company's consolidated balance sheet.

Meetings and attendance table

	Board	Audit Committee	Remuneration Committee	Nominations and Governance Committee
Director	Attended	Attended	Attended	Attended
Robert Childs	4/4	N/A	N/A	4/4
Bronek Masojada	4/4	N/A	N/A	N/A
Aki Hussain	4/4	N/A	N/A	N/A
Richard Watson	4/4	N/A	N/A	N/A
Caroline Foulger	4/4	4/4	4/4	4/4
Michael Goodwin	4/4	4/4	4/4	4/4
Thomas Hürlimann	4/4	4/4	4/4	4/4
Colin Keogh	4/4	4/4	4/4	4/4
Anne MacDonald	3/4	3/4	3/4	3/4
Bob McMillan	4/4	4/4	4/4	4/4
Costas Miranthis	4/4	4/4	4/4	4/4
Lynn Pike	4/4	4/4	4/4	4/4

The Chief Actuary presented a Group reserving report to the Committee, which reviewed the approach taken by management when making its selection of reserving estimates. The Committee is satisfied with the judgements taken and the reporting and disclosure of these estimates.

During the year, a number of natural catastrophes occurred, including Hurricanes Florence and Michael, Typhoons Jebi and Trami, and unprecedented wildfires in California. The Committee received an update on the processes that the Company conducts when significant events, such as the California wildfires, arise. It is imperative that the Company can quickly, and to a reasonable degree of accuracy, estimate the gross and net losses arising from such events. The Committee is satisfied with the way that the process was conducted.

ii) The carrying value of deferred tax

As explained in note 2.21, a deferred tax asset has been established relating to operating losses arising in foreign subsidiaries. The recoverability of these assets is dependent upon the future profitability of these subsidiaries. The Committee reviewed the methodology used by management to assess the projected profitability and the carrying amount of the deferred tax asset and is satisfied with the methodology.

iii) The valuation of the investment portfolio

The Group reports its assets at fair value. As discussed in note 2.21, during periods of economic stress, the resulting diminished liquidity means that estimating fair value involves a higher level of judgement. The Committee has evaluated the process used by management to estimate the fair value of the investment portfolio and is satisfied with their conclusions.

iv) Accounting for the defined benefit scheme

As explained in note 2.15, the Group recognises the present value of the defined benefit obligation, less the fair value of plan assets at the balance sheet date. The Audit Committee reviewed the report of the key judgements and estimates in the financial statements from the Chief Financial Officer, and the results of the independent pension valuation, and is satisfied that the assumptions used to measure the deficit are reasonable.

v) The recoverability of reinsurance assets

As a result of the large loss activity in the year, the level of exposure to reinsurers has increased. The Committee received an update on the process to monitor the levels of recoverability, including the level of collateral held, and the regular contact with counterparties. The Committee is satisfied with the approach taken and the recoverability of those assets.

Changes in presentation currency and functional currency

Following the change in the functional currency of a number of trading subsidiaries and the Group's presentation currency to US Dollars with effect from 1 January 2018, the Group has performed a historic retranslation of the Group's results. See note 2.1 for further detail.

The Committee reviewed the key accounting and disclosure impacts in relation to both changes and received reports from the external auditors with their assessment of the accounting treatment and disclosures in the financial statements.

After having reviewed these reports and the disclosures in the financial statements, the Committee concluded that it was satisfied with the accounting treatment and disclosure for each of these matters.

Finance transformation programme (FTP)

The Company continued with its finance change initiatives, which involves a wide-ranging transformation of the finance IT systems and controls. The head of the FTP provides a quarterly update to the Committee on the status of the project.

UK Corporate Governance Code

In accordance with the 2016 UK Corporate Governance Code, the Board requested that the Committee advise on whether it believes the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy. The Committee has provided such advice to the Board.

External auditor

PwC was appointed as the Group's auditor at the 2016 Annual General Meeting following a tender exercise that commenced in 2014 and was reported on in the 2015 Annual Report and Accounts.

The external auditor is invited to attend all meetings of the Committee and it is the responsibility of the Committee to monitor their performance, objectivity and independence. The Committee discusses and agrees with the auditor the scope of the audit plan for the full-year and the review plan for the interim statement.

The Audit Committee receives reports from the external auditor at regular intervals during the audit process, including those relating to the judgements outlined above. The external auditor provides reports at each Committee meeting on topics such as the control environment, key accounting matters and mandatory communications. Any contracts with PwC for non-audit services in excess of £50,000 must be approved by the Committee in advance. It is Group policy not to approve any contract that may impair the auditor's independence or objectivity.

During the year, the value of non-audit services provided by PwC amounted to $168,000 (2017: $257,000). There were no circumstances in which PwC was engaged to provide services that might have led to a conflict of interests, nor does the Audit Committee consider the quantum of the fees impacts the independence of the auditor. To provide a forum in which any matters of concern could be raised in confidence, the Non Executive Directors met with the external and internal auditors throughout the year without the Executive Directors present.

Internal audit

The Group Head of Internal Audit is invited to attend all meetings of the Committee. It is the responsibility of the Committee to monitor and review the effectiveness of the Group's internal audit function and to consider reports prepared by internal audit on the effectiveness of systems of internal control.

Group Risk Officer

The Group Risk Officer is also invited to attend all meetings of the Committee. The Company has in place a Risk Committee and the items discussed by the two Committees can overlap, therefore the attendance of the Group Risk Officer aids in facilitating discussions relating to risk.

Caroline Foulger
Chairman of the Audit Committee

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Remuneration

Letter from Chairman of the Remuneration Committee

Dear fellow Shareholder
At Hiscox, our aim is to deliver strong returns across the insurance cycle and create sustainable long-term value for our shareholders. This requires us to attract and retain good people and provide them with the means and motivation to excel. To achieve this, our philosophy is a simple one: to reward performance. For over a decade, the foundation of the Group's remuneration strategy has been the belief that the best way to foster a high-performance culture across the Group is to ensure that pay reflects our results, not just effort.

The Remuneration Committee believes that base remuneration should be competitive but not excessive, with outperformance rewarded through variable pay.

Incentives require demanding performance targets to be met. The outcomes from bonus and long-term share awards reflect the part played in delivering profits in excess of a specified return threshold and value we create for our shareholders.

What we demand of our executives also goes beyond financial performance. We expect all employees to meet or exceed a series of non-financial targets, consistent with our strategy and values. These include delivering great service to customers, complying with regulation and managing risk, all of which are core to the business operations and reputation of Hiscox.

We believe that our remuneration principles work well for our employees and shareholders. Over the last three years, the total return on Hiscox shares was 67%, three times that of the FTSE All-Share Index.

The following principles define our approach to remuneration

- Simple and strictly results-driven, with variable rewards only if Hiscox delivers profits in excess of a specified return threshold.
- Incentivise Executive Directors appropriately, over the short and long term.
- Align Executive Directors' interests with those of our shareholders, focusing on effective risk management, ROE and net asset value growth, which drive total shareholder return over time.

Performance and remuneration outcomes

Hiscox delivered an underwriting profit of $170.5 million (2017: $71.3 million), a total dividend of 41.85¢ and pre-tax ROE of 6.0% amid a second year of significant natural catastrophes, financial market turmoil and geopolitical uncertainty. The business also made good progress on a number of operational initiatives during 2018, including completing preparations for Brexit, adapting to GDPR, upgrading major IT infrastructure and modernising our finance function. This result demonstrates the resilience of Hiscox and the success of our long-held strategy.

For 2018, the pre-tax ROE bonus hurdle rate of 6% was achieved therefore a bonus pool was created and, in line with the pre-disclosed bonus ranges, this level of performance enabled Executive Directors to be considered for bonus awards.

In considering bonus awards, the Committee took account of the personal performance of the individuals, the size of the bonus pool and the overall performance of Hiscox, including strong underwriting performance, good growth and improved ROE. As such, the three Executive Directors were awarded bonuses representing 9% of the maximum opportunity. This is in line with our approach of rewarding financial outcomes, not just effort. For the wider workforce, we paid bonuses relative to personal performance and profitability of business area.

The long-term incentive plan (LTIP) award granted in 2016 will vest at 47% of maximum. Over the last two years natural catastrophes have impacted our performance which has driven a three-year average post-tax ROE of 9.24%, the key metric for determining this award under the Performance Share Plan. The vesting outcomes for Executive Directors are lower than in recent years, however, the Committee believes that they are aligned with the experience of shareholders.

The net result of the above is that the remuneration package and single figure result reported for the Chief Executive is lower than previous years. In 2018, the Chief Executive's single figure was £1,862,710, a decrease of 22%.

Improved disclosure

The latest version of Hiscox's remuneration policy on pages 84 to 93 was approved at the 2017 Annual General Meeting. In last year's report we noted that following discussions with shareholders and in direct response to feedback from prior years, a number of improvements were to be made to how the policy would be implemented and reported in 2018.

The changes outlined in last year's report comprised a commitment to increased transparency regarding bonus outcomes, including both prospective and retrospective disclosure of pre-tax ROE targets; use of growth in net asset value plus dividends measured on a per share basis for future Performance Share Plan awards; and an increase to the minimum shareholding guidelines for our Executive Directors.

This approach was positively received by our shareholders at the 2018 AGM and therefore no major changes are proposed in this year's report. We intend to largely maintain this approach for the coming year.

Corporate governance developments

The new UK Corporate Governance Code ('the Code') comes into effect during 2019. The Remuneration Committee is supportive of much of the guidance and clarity that the new regime will bring in relation to remuneration matters. The Committee believes that Hiscox complies with the spirit of the Code, and we have adopted some of the specific requirements early.

Pension benefits for Executive Directors at Hiscox have always been consistent with the wider UK workforce. All three Executive Directors received a 10% cash allowance in lieu of the standard employer pension contribution. Like other long-serving employees, the Chief Executive and Chief Underwriting Officer have legacy entitlements under a defined benefit scheme and no further accruals are available under this plan.

The Committee already monitors market practice and receives a variety of information on wider workforce pay policies, including information on aggregate workforce pay and gender pay analysis. We are now improving visibility of remuneration metrics across the Group through a regularly updated dashboard. This new responsibility has also been added to the Committee's formal Terms of Reference.

Remuneration Committee responsibilities

The responsibilities of the Remuneration Committee include:

- ensuring the remuneration policy of the Company encourages enhanced performance and in a fair and responsible way, rewards individuals for their contribution to the Company's success;
- ensuring workforce remuneration, incentives and rewards are aligned with culture;
- setting, and agreeing with the Board, the remuneration of the Chairman and Executive Directors of the Company, including pension rights and any compensation payments. Doing so addresses the requirements of the UK Corporate Governance Code for clarity, simplicity, risk, predictability, proportionality and alignment to culture;
- approving performance-related pay schemes and their total annual payments;
- making recommendations on the structure of share incentive plans and determine awards to Executive Directors and senior management.

We have opted to provide disclosure on our Chief Executive's pay ratios on a voluntary basis in this year's report. We expect the ratios to be volatile year-on-year due to the variable and performance-based nature of the Chief Executive's remuneration package. While the ratio needs to be understood within the context of our business, it does provide a further reference point for the Committee. This is outlined on page 81.

Hiscox published its second gender pay gap report for the UK in 2018, which showed a small year-on-year improvement in our median pay gap. The pay gap between men and women remains higher than we would like, at 24.5% (2017: 26.2%), which is mainly driven by the fact that, similar to many organisations, we have fewer women than men in more senior, higher-paid roles. We continue to work hard to address this, with diversity and inclusion remaining a strategic priority for the Executive Committee in 2019. Our work on diversity and inclusion is outlined on page 56.

Looking ahead

The Remuneration Committee is satisfied that our practices are aligned with the interests of shareholders and incentivise Directors appropriately over the short and long term, and we remain committed to the principles that have underpinned our remuneration strategy for over a decade. Under the normal three-year renewal cycle, the remuneration policy is next due for approval by our shareholders at the 2020 AGM, and we will review our approach against evolving market and best practice in advance of this.

We value the views of our shareholders and we will seek to maintain dialogue to ensure there is clarity regarding the decision-making of the Committee. Together with the rest of the Board, I look forward to receiving your approval and hearing your feedback at our 2019 AGM.

Colin Keogh
Chairman of the Remuneration Committee

Remuneration summary

Key principles underpinning remuneration at Hiscox

The Hiscox remuneration policy is designed to drive a culture of high performance and create sustainable long-term value for shareholders. The policy follows three clear principles:

- Simple and strictly results-driven, with variable rewards only if Hiscox delivers profits in excess of a specified return threshold.
- Incentivise Executive Directors appropriately, over the short and long term.
- Align Executive Directors' interests with those of our shareholders, focusing on effective risk management, ROE and net asset value growth, which drives total shareholder return over time.

Remuneration outcomes for 2018

Hiscox more than tripled profits to $137.4 million in what was a difficult year for insurers.

Bonus of 9% of maximum opportunity for Executive Directors.

Long-term performance impacted by catastrophes with ROE of 9%. PSP awards granted in 2016 vested at 47% of maximum.

Single figure of £1,862,710 for CEO, is 22% lower than last year.

Summary of remuneration arrangements for 2019

A summary of the remuneration arrangements for Executive Directors is provided opposite, the remuneration policy is detailed on pages 84 to 93.

As detailed in the 2017 Remuneration Committee Chairman's letter, certain changes were made last year to the implementation of the policy approved at the 2017 AGM in response to shareholder feedback. The remuneration policy is due for renewal at the 2020 AGM.

84-93

Base salary

Competitive but not excessive.

Benefits

Same as majority of employees.

Annual bonus

Aligned to shareholder interests.

Performance Share Plan (PSP)

Aligned to long-term shareholder interests and performance.

Shareholding guidelines

Aligned to shareholder interests.

Implementation policy for 2018	Implementation policy for 2019
Salaries for 2018: —— Bronek Masojada: £620,000 —— Aki Hussain: £477,000 —— Richard Watson: £477,000 Salary increase of 3.4%, in line with average UK employee increase.	Salaries for 2019: —— Bronek Masojada: £636,500 —— Aki Hussain: £490,000 —— Richard Watson: £490,000 Salary increase of 2.7%, in line with the average UK employee increase.
Executive Directors' benefits can include health insurance, life insurance, long-term disability schemes and participation in all-employee share schemes. Retirement benefits are delivered via a cash allowance of 10% of salary, paid in lieu of the standard pension contribution. These benefits mirror those available to most other employees in the organisation.	
Maximum opportunity: —— up to 400% of salary for CEO and CFO; —— up to 500% of salary for CUO. Over the past ten years, the average bonus to the CEO has been equivalent to c.35% of the current maximum opportunity. **Performance metrics:** combination of ROE and individual performance delivered against set objectives approved by the Board. **Deferral:** part deferral of amounts in excess of £50,000. **2018 actual as percentage of salary (9% of maximum opportunity):** —— Bronek Masojada: 36% —— Aki Hussain: 36% —— Richard Watson: 45%	Operation of annual bonus unchanged.
Award subject to three-year performance period and two-year holding period. **Maximum opportunity:** 200% of salary for all Executive Directors. **Vesting subject to:** net asset value per share growth plus dividends. 20% vests for achievement of threshold performance, 100% of maximum. **2018 actual as percentage of salary:** —— Bronek Masojada: 200% —— Aki Hussain: 181% —— Richard Watson: 181%	Vesting criteria unchanged.
Share ownership guidelines of 200% of salary for all Executive Directors, after five years in role. **2018 actual:** —— Bronek Masojada: 7,300% —— Aki Hussain*: 200% —— Richard Watson: 1,900% *Aki Hussain was appointed in September 2016.	Share ownership guidelines unchanged.

Annual report on remuneration 2018

This report explains how the remuneration policy was implemented for the financial year ending 31 December 2018 and how it will be applied for the 2019 financial year.

PwC has been engaged to audit the sections in the annual report on remuneration 2018 below entitled 'Executive Director remuneration' and additional notes, 'annual bonus', 'long-term incentives', 'details of pension entitlements', 'Non Executive Director remuneration', 'Directors' shareholding and share interest', 'Performance Share Plan' and 'Sharesave Schemes', 'Payments for loss of office or payments to past Directors, to the extent that would be required by the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2013.

Executive Director remuneration

2018

Name	Salary £	Benefits[4] £	Bonus[1] £	Long-term incentives[2] £	Retirement benefits £	Total £
Bronek Masojada	614,906	9,971	223,000	960,799	54,034	1,862,710
Richard Watson	473,063	10,211	215,000	662,950	43,004	1,404,228
Aki Hussain[3]	473,063	7,338	172,000	597,465	43,004	1,292,870

2017

Name	Salary £	Benefits[4] £	Bonus[1] £	Long-term incentives plan[2] £	Retirement benefits £	Total £
Bronek Masojada	595,969	9,720	0	1,736,369	52,370	2,394,428
Richard Watson	458,438	9,367	0	1,298,263	41,674	1,807,742
Aki Hussain[3]	458,438	7,128	0	512,900	41,674	1,020,140

[1] A proportion of the bonus amount is deferred as set out on page 87 of the policy report.
[2] 2018 long-term incentives relate to performance share awards granted in 2016, or on joining in the case of Aki Hussain, where the performance period ends on 31 December 2018. The award is due to vest on 8 April 2019. The amount also includes dividend equivalents accrued on this award. For the purpose of this table the performance share award has been valued based on the average share price during the three-month period to 31 December 2018 of 1,621.30p. Of the vested amount, over 75% relates to share price appreciation over the performance period (60% for Aki Hussain).
The 2017 long-term incentive award relates to performance share awards granted in 2015 where the performance period ended on 31 December 2017. The amount also includes dividend equivalents accrued on this award. For the purpose of this table the performance share award has been valued based on the share price on 13 April 2018 of 1484.00p resulting in an increase of £218,031 to the previously reported amount based on the Q4 2017 average share price.
[3] Aki Hussain was appointed 12 September 2016. Details of his joining package are in the 2016 remuneration report.
[4] In addition to these benefits there is an inherent gain at grant under the Sharesave Scheme. The interests of Executive Directors under the Sharesave Schemes are set out on page 79.

Additional notes to the Executive Director remuneration table

Salary

Salary reviews take place in the first quarter of the year, effective from 1 April. As noted in last year's remuneration report, Executive Directors' salaries were increased by 3.4% from April 2018, the same as the average UK-based employee salary increase.
Base salaries for Executive Directors from 1 April 2018 were as follows:

	April 2018
Bronek Masojada	£620,000
Richard Watson	£477,000
Aki Hussain	£477,000

Benefits
For 2018, benefits provided for Executive Directors included the Company healthcare scheme, life insurance, income protection insurance and critical illness policies as well as a Christmas gift hamper and Sharesave Scheme.

Variable pay
To ensure that remuneration is aligned with Company performance and the shareholder experience, a significant proportion of pay is delivered through incentive awards, consisting of an annual bonus and share awards under the Performance Share Plan, which can vary significantly based on the level of performance achieved. Variable pay awards are only paid if results exceed a specified threshold and are not used as a reward for effort alone – an approach that has helped reinforce a strong performance culture across the business.

Although the remuneration structure has naturally evolved over time to reflect market and best practice, the simple framework has been in place for more than 15 years.

Annual bonus
In response to shareholder feedback the Committee has once again sought to improve the transparency around the process for determining bonuses.

Structure of bonus
The bonus is structured in a way that ensures significant variability in outcomes, including the possibility of no bonus being paid where performance thresholds are not achieved. For example, in 2017 the share price increased by more than 40%, however no bonuses were paid to Executive Directors as performance thresholds were not met. The Remuneration Committee believes that the most appropriate measure for the calculation of the bonus pool is pre-tax return on equity (ROE), as this aligns management's interests with those of shareholders, minimises the possibility of anomalous results, and ensures that incentives for Executive Directors and other employees are tied to the Company's profit performance.

The Executive Directors, along with other employees across the Group, participate in profit-related bonus pools, which are calculated at a business unit level and for the Group as a whole. In determining the bonuses to be paid to Executive Directors, the Remuneration Committee bases its judgement on both the performance of the Group and a robust assessment of individual performance, including adherence to specific risk management objectives. The Remuneration Committee also seeks input from the Chief Risk Officer and Chief Actuary to aid its assessment of whether bonus outcomes are appropriate.

Bonuses are not paid unless the Group's performance exceeds a given threshold, irrespective of individual performance. Over the past ten years there have been two occasions when the Group delivered a pre-tax ROE below the required threshold and no bonuses were paid to Executive Directors.

When setting targets, the Committee seeks to motivate strong performance while also encouraging sustainable behaviours, in line with the defined risk appetite of the business. In determining the size of the Executive Director bonuses, the Committee uses the following framework:

Pre-tax return on equity	Indicative bonus range (% of max)
Less than RFR* +<5%	Nil
RFR +5% to RFR +12.5%	0-15%
RFR +10% to RFR +17.5%	15-40%
RFR +15% to RFR +22.5%	30-60%
RFR +20% to RFR +25%	50-70%
Greater than RFR +22.5%	60-100%

*Risk-free rate.

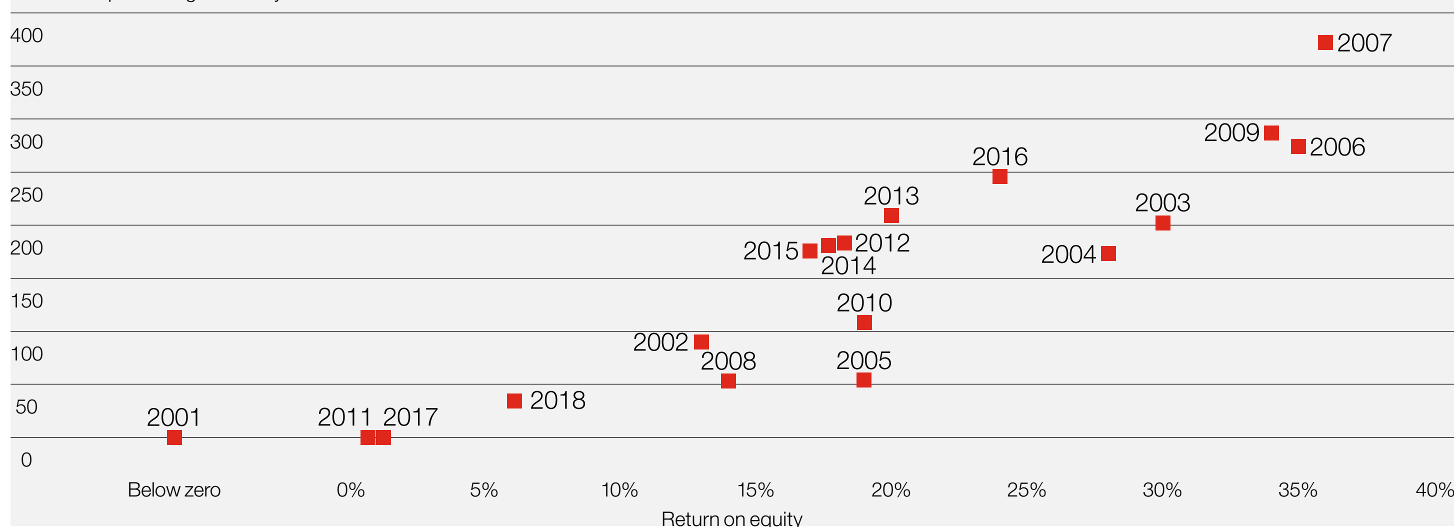
Junior and mid-level employees also participate in a personal performance bonus scheme. Awards under this scheme are based entirely on individual performance ratings. It is designed to ensure that junior and mid-level employees continue to be motivated to perform well, irrespective of overall Group performance. The benefit is up to 10% of salary.

Pay for performance – track record

The chart below shows the relationship between the Group ROE performance and bonus awards for Executive Directors over an extended period. It demonstrates the strong link between Company performance and bonus outcomes.

Executive Directors' cash incentives and return on equity

Bonus as a percentage of salary



Performance outcomes for 2018

2018 was another challenging year for insurers. After a relatively benign start, a number of natural catastrophes and significant large losses in the second half, combined with turbulent financial markets, impacted the industry. In these circumstances, the Group delivered a good profit before tax of $137.4 million and showed strong growth in gross premiums written of 15.0%.

As outlined earlier, bonuses are only paid when pre-tax ROE reaches 5% plus the risk-free rate, irrespective of outstanding individual performance. If the threshold is met, the Committee awards individual bonuses guided by the framework set out on page 73.

For 2018, the pre-tax ROE bonus hurdle rate of 6% was achieved therefore a bonus pool was created and, in line with the pre-disclosed bonus ranges, this level of performance enabled Executive Directors to be considered for bonus awards. In considering bonus awards, the Committee took account of the personal performance of the individuals, the size of the bonus pool and the overall performance of Hiscox, including strong underwriting performance, good growth and improved ROE. As such, the three Executive Directors were awarded bonuses representing 9% of maximum opportunity. This is in line with our approach of rewarding financial outcomes, not just effort. For the wider workforce, we paid bonuses relative to personal performance and profitability of business area.

Executive Directors are set stretching individual objectives that are aligned to the strategy and long-term goals of the business.

All of the Executive Directors performed strongly against these objectives in 2018.

Some key objectives and individual achievements by the Executive Directors are outlined below.

	Key objectives	Achievements
Bronek Masaojada	Delivering the business plan	The business had strong growth across all business units, growing by 15%, with improving profits and reasonable RoE given the market environment.
	Lead Brexit adaptation project	The Brexit project was chaired by Bronek and put in place new structures allowing Hiscox to serve customers in any Brexit outcome. These include: a new insurance company in Luxembourg; a Part VII process to transfer policyholder liabilities to the new entity; and adapting to the use of Lloyd's Brussels. The project was delivered in time for 2019.
	Deliver on risk and regulatory objectives	Bronek oversaw projects to materially adapt Hiscox to new regulatory expectations such as GDPR and SMCR.
	Lead evolution of senior roles	Bronek ensured a key transition as Steve Langan moved to Hiscox USA, from Hiscox UK, to become its new CEO, and Ben Walter moved to the UK as the newly created CEO of Hiscox Global Retail. Bronek also recruited Grace Hanson as Head of Claims in succession to Jeremy Pinchin.
Richard Watson	Reinsurance purchase	Richard has successfully hedged the underwriting portfolio through the purchase of a reinsurance program that delivers the net risk profile agreed by the Board. The reinsurance spend of circa $1 billion encompasses the traditional reinsurance market, and newer ILS and non-traditional partners. The Group maintained core reinsurer partnerships, matched its defined credit risk profile, and developed an efficient transfer of risk.
	Underwriting talent	Richard has championed new ways to identify, retain and develop the best underwriting talent, raising the bar on what Hiscox looks for in underwriters.
	Data	Richard has developed a centre of excellence at a Group level to accelerate better use of data. Consequently, the business units are investing in new capabilities and driving genuine competitive advantage in areas as diverse as UK direct to US flood risks.
	Third-party capital	Richard has been instrumental in driving a strategy of how much, and where, we use third-party capital, maintaining Hiscox's relevance in the market. As a result, Hiscox is attractively positioned with a combination of quota shares, ILS funds, consortia and a track record of managing capacity responsibly, and transparently. 2018 saw the funds and facilities grow and a push to develop ILS funds into the insurance market.
Aki Hussain	Optimising liquidity	Aki has improved liquidity management processes. In addition during the year, the Group completed a $380 million bond issuance. This further optimised the Group's liquidity position, giving it the strategic flexibility to react to changing market conditions and seize profitable growth opportunities as they arise.
	Optimising capital	Aki has developed a new capital management philosophy and improved the Group's overall capital position through a range of internal initiatives, supporting increased premium growth. In addition he has improved the rating agency capital position, specifically after an extended period of consultation with S&P, which had been the Group's biting capital constraint. S&P issued a risk re-classification for Hiscox from high to moderate risk, reflecting the diversification benefit of the retail businesses.
	Modernising our finance function	Aki has made good progress in evolving the processes, professionalism and commerciality of the finance function. This includes upgrading core finance systems, improving financial control environment, making preparations for IFRS 17 and a focus on capital efficiency.

Long-term incentives

Performance Share Plan awards (PSP) where the performance period ends with the 2018 financial year

Bronek Masojada and Richard Watson were granted nil cost options under the PSP in 2016 for the three-year performance period 1 January 2016 to 31 December 2018. As outlined in the 2016 Directors' remuneration report, Aki Hussain was granted a buy-out award under his appointment terms, which is based on the same performance criteria.

The performance conditions for these awards were as follows:

	Required average post-tax ROE over three-year performance period %	Proportion of PSP vesting %
Minimum threshold vesting	Expected investment return + 5 = 7	25
Maximum vesting	Expected investment return + 12.5 = 14.5	100
Straight-line vesting between these points		

Performance outcome

Our three-year average post-tax ROE of 9.24%, the key metric for determining this award under the Performance Share Plan, has been impacted by the natural catastrophe activity of the last two years. The LTIP award granted in 2016 will vest at 47% of maximum. The vesting outcomes are lower than in recent years, however the Committee believes that the vesting outcomes are aligned with the experience of shareholders. Executive Directors will also receive dividend equivalents in the form of additional awards based on dividends paid during the three-year performance period. The estimated value of these awards is covered in the Executive Director remuneration table on page 72.

PSP awards granted during the 2018 financial year

On 6 April 2018, Bronek Masojada, Richard Watson and Aki Hussain were granted nil cost options under the PSP.

	Percentage of salary	Number of awards granted	Mid-market price on date of grant	Market value at date of grant
Bronek Masojada	200%	83,250	14.88	1,238,760
Richard Watson	181%	58,000	14.88	863,040
Aki Hussain	181%	58,000	14.88	863,040

The performance conditions for these awards are as follows:

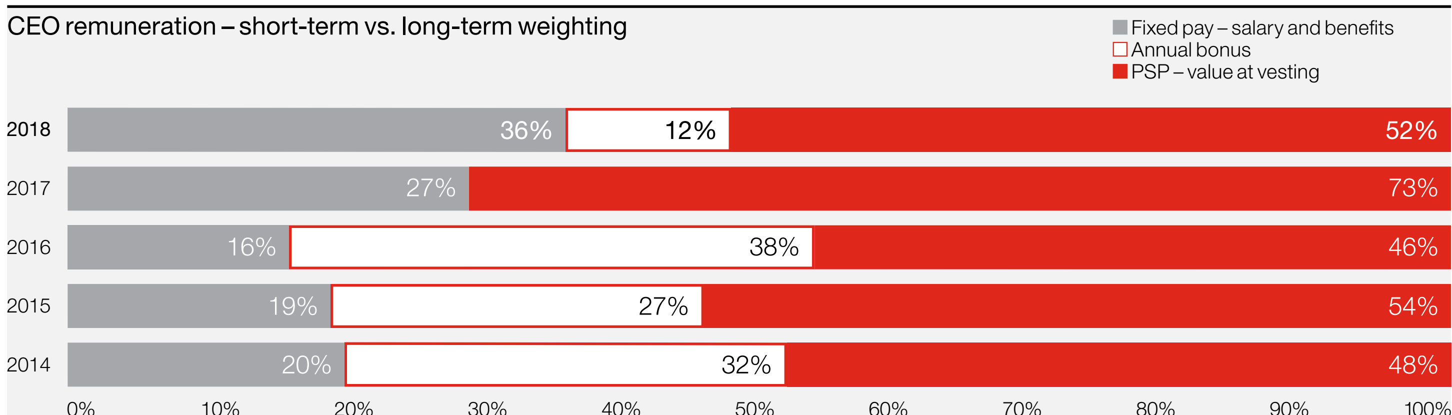
	Growth in net asset value plus dividends measured on a per share basis	Proportion of PSP vesting %
Minimum threshold vesting	RFR + 6 = 7	20
Maximum vesting	RFR + 14 = 15	100
Straight-line vesting between these points		

The net asset value targets, which are reviewed annually, are designed to outperform the risk-free rate (RFR) and motivate the management team while driving the right behaviours.

The vest date is 6 April 2021. Executive Directors will be required to retain any shares vesting (net of tax charges) at the end of the performance periods for a further two years (five years post the start of the performance period).

Balance between pay elements

The chart below shows the balance between fixed pay, annual variable pay and long-term variable pay for the CEO over the past five years. The value of vested PSPs has been the material element of the CEO's remuneration. Good performance and share price appreciation has increased the value of PSPs over time. For example, the PSP award with a performance period ending in 2016 had a value at grant of £1,082,640 and at vesting was £1,826,470.



Details of pension entitlements

All open Hiscox retirement schemes are based on defined contributions. Bronek Masojada, Richard Watson and Aki Hussain hold lifetime allowance protection certificates and have therefore opted out of the Company pension scheme. They receive a 10% cash allowance (less an offset for the employer's UK National Insurance liability) in lieu of the standard employer pension contribution. The value of this benefit is shown in the Executive Director remuneration table on page 72. As noted above, and consistent with the 2018 UK Corporate Governance Code, the retirement benefits are consistent with those offered to the majority of UK employees. This has been the policy at Hiscox for a number of years.

The table below details the legacy entitlements from the defined benefit pension plan. There are no further accruals under this plan.

Pensions	Normal retirement age	Increase in accrued pension during the year £000	**Total accrued annual pension at 31 December 2018 £000**	Increase in accrued pension net of inflation £000	Transfer value of accrued pension at 31 December 2017 £000	**Transfer value of accrued pension at 31 December 2018 £000**	Increase/(decrease) in transfer value of accrued pension during the year £000
Bronek Masojada	60	3	**55**	–	2,073	**2,107**	34
Richard Watson	60	10	**176**	–	6,978	**7,092**	114

In the event of early retirement the Directors receive a reduced pension to reflect early payment in accordance with the scheme rules.

Non Executive Director remuneration

The table below sets out the remuneration received by the Non Executive Directors for the financial years ending 31 December 2018 and 31 December 2017. Non Executive Director fees were reviewed in 2018 and some were subsequently increased. There are no further increases currently proposed to Non Executive Director fees for 2019.

	2018					2017				
	Ltd Board fee £	Ltd Committee fee £	Subsidiary Board fee £	Benefits[1] £	Total Hiscox fees £	Ltd Board fee £	Ltd Committee fee £	Subsidiary Board fee £	Benefits £	Total Hiscox fees £
Robert Childs	145,000	–	145,000	11,301	301,301	140,000	–	140,000	11,203	291,203
Caroline Foulger	64,662	35,338	87,846	–	187,846	65,167	34,135	86,126	–	185,428
Michael Goodwin[2]	64,662	27,820	–	–	92,482	8,146	3,297	–	–	11,443
Thomas Hürlimann[2]	64,662	27,820	40,254	–	132,736	8,146	3,297	–	–	11,443
Colin Keogh	76,692	34,211	15,567	–	126,470	77,580	32,196	–	–	109,776
Anne MacDonald	64,662	27,820	–	–	92,482	65,167	26,377	–	–	91,544
Robert McMillan	64,662	31,579	60,150	–	156,391	65,167	26,877	62,064	–	154,108
Constantinos Miranthis[2]	64,662	27,820	19,825	–	112,307	8,146	3,297	–	–	11,443
Lynn Pike	64,662	33,083	–	–	97,745	65,167	31,808	–	–	96,975

[1] Benefits include life assurance and healthcare.
[2] Appointed 16 November 2017.

2018 fees that were paid in US Dollars have been converted using an exchange rate of 1.33. Those paid in Euros were converted using 1.18.
2017 US Dollar fees were converted using 1.289.

Directors' shareholding and share interests

To align their interests with those of Hiscox shareholders, senior managers are expected to own a minimum number of Hiscox shares. Executive Directors are required to hold Hiscox shares valued at 200% of salary within five years of becoming an Executive Director. Bronek Masojada and Richard Watson have over 20 and 30 years' service respectively, so their shareholdings far exceed the guidelines. Aki Hussain was appointed to the Board in September 2016 and will be expected to a build a shareholding in the Company over the course of his tenure.

Under the Company's existing PSP, awards to good leavers are generally released at the end of the normal performance period and therefore Directors generally retain a significant interest in Company shares after they leave the Company. As part of the renewal process of the remuneration policy in 2020, the Committee will give further consideration to how Executives remain aligned with the performance of the business following departure.

The interests of Executive and Non Executive Directors are set out below, including shares held by connected persons. There have been no changes in the Director share interests between 31 December 2018 and 26 February 2019.

Directors	31 December 2018 6.5p ordinary shares number of shares beneficial	31 December 2017 6.5p ordinary shares number of shares beneficial
Executive Directors		
Bronek Masojada	3,014,894	3,064,702
Richard Watson	614,973	691,973
Aki Hussain	64,794	19,700
Non Executive Directors		
Robert Childs	1,274,610	1,379,610
Caroline Foulger	8,231	8,077
Michael Goodwin	4,986	4,950
Thomas Hürlimann	3,682	–
Colin Keogh	20,942	17,016
Anne MacDonald	28,611	22,185
Robert McMillan	–	–
Constantinos Miranthis	4,525	–
Lynn Pike	–	–

Performance Share Plan (PSP)

Awards in the form of nil-cost options are granted under the PSP as a percentage of salary. All awards are subject to performance conditions. The interests of Executive Directors are set out below:

	Number of awards at 1 January 2018	Number of awards granted	Number of awards lapsed	Number of awards exercised	Number of awards at 31 December 2018	Mid market price at date of grant £	Market price at date of exercise £	Date from which released
Bronek Masojada	168,450	–	–	–	168,450	6.94		17-Mar-17*
	130,000	6,116	(19,110)	–	117,006	8.82		13-Apr-18*
	120,000	–	–	–	120,000	9.56		08-Apr-19
	105,000	–	–	–	105,000	11.19		07-Apr-20
	–	83,250	–	–	83,250	14.88		06-Apr-21
Richard Watson	10,000	–	–	(10,000)	–	6.94	14.94	17-Mar-17
	97,200	4,573	(14,289)	–	87,484	8.82		13-Apr-18*
	82,800	–	–	–	82,800	9.56		08-Apr-19
	75,000	–	–	–	75,000	11.19		07-Apr-20
	–	58,000	–	–	58,000	14.88		06-Apr-21
Aki Hussain	50,787	–	–	(50,787)	–	10.46[1]	16.67	17-Mar-17
	39,709	691	(5,838)	(34,562)	–	10.46[1]	16.67	13-Apr-18
	75,000	–	–	–	75,000	10.46[1]		08-Apr-19
	75,000	–	–	–	75,000	11.19		07-Apr-20
	–	58,000	–	–	58,000	14.88		06-Apr-21
Total	1,028,946	210,630	(39,237)	(95,349)	1,104,990			

[1] Grants made on 12 September 2016. Details of Aki Hussain's joining package are in the 2016 remuneration report.
*Awards have vested but are unexercised.

Sharesave Schemes

The interests of Executive Directors under the Sharesave Schemes are set out below:

The scheme offers a three-year savings contract where the exercise price of the options is calculated based on an average share price over five days prior to the invitation date, with a 20% discount.

	Number of options at 1 January 2018	Number of options granted	Number of options lapsed	Number of options exercised	Number of options at 31 December 2018	Exercise price £	Market price at date of exercise £	Date from which exercisable	Expiry date
Bronek Masojada	1,040	–	–	–	**1,040**	8.648		01-Jun-20	30-Nov-20
	–	778	–	–	**778**	11.556		01-Jun-21	30-Nov-21
Richard Watson	–	1,557	–	–	**1,557**	11.556		01-Jun-21	30-Nov-21
Aki Hussain	2,081	–	–	–	**2,081**	8.648		01-Jun-20	30-Nov-20
Total	3,121	2,335	–	–	**5,456**				

External Non Executive Directorships

Executive Directors may not accept any external appointment that may give rise to a conflict of interest, and all external appointments require the consent of the Chairman. During the year Bronek Masojada held Directorships on the Board of the Association of British Insurers, Bajka Investments (Pty) Ltd, Heptagon Assets Ltd, Heptagon BIR Ltd and Pool Reinsurance Company Limited and was Chair of Policy Placement Limited. He was not remunerated for his services. Richard Watson held a Directorship at White Oak Underwriting Agency Limited. He was not remunerated for his services.

Table of historic data

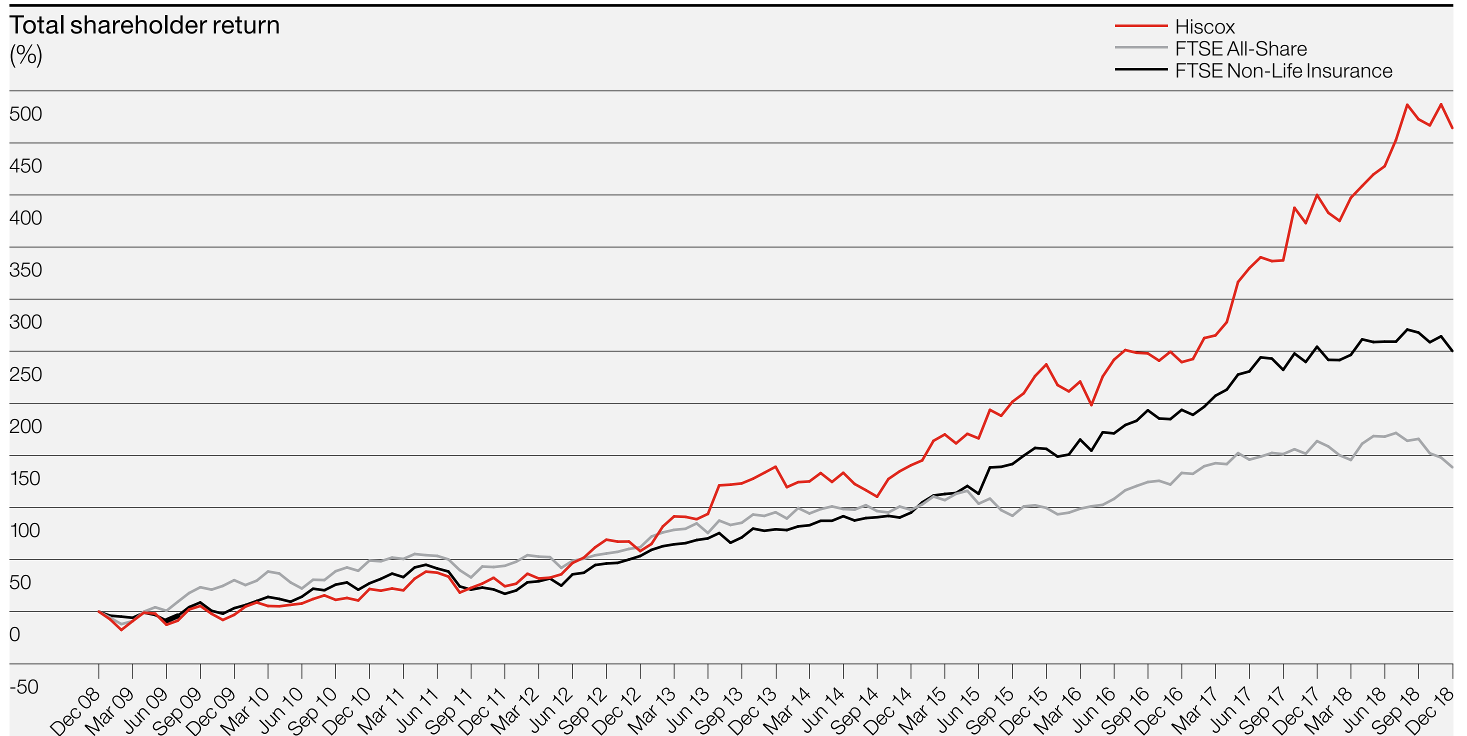
The table below shows the single total remuneration figure for the Chief Executive for the past ten years.

	2009	2010	2011	2012	2013	2014	2015	2016	2017	**2018**
CEO single figure of remuneration (£)	2,536,943	1,759,123	1,509,248	1,938,759	2,341,737	3,130,535	3,358,894	3,970,466	2,394,428	**1,862,710**
Annual bonus as percentage of current max	71	29	0	46	51	44	39	64	0	**9**
PSP vesting as percentage of maximum opportunity	100	100	85	39	53	100	100	100	85	**47**

Prior to 2015 the annual bonus was operated on an uncapped basis. In order to facilitate comparison the current 400% salary cap has been applied retrospectively.

Total shareholder return performance

The graph below shows the total shareholder return of the Group against the FTSE All-Share and FTSE Non-Life Insurance indices. These reference points have been shown to assess performance against the general market and industry peers. Between December 2008 and 2018, Hiscox delivered total shareholder return of 464.3% – well above the FTSE All-Share and FTSE Non-Life Insurance indices.



Percentage change in remuneration of Director undertaking the role of Chief Executive

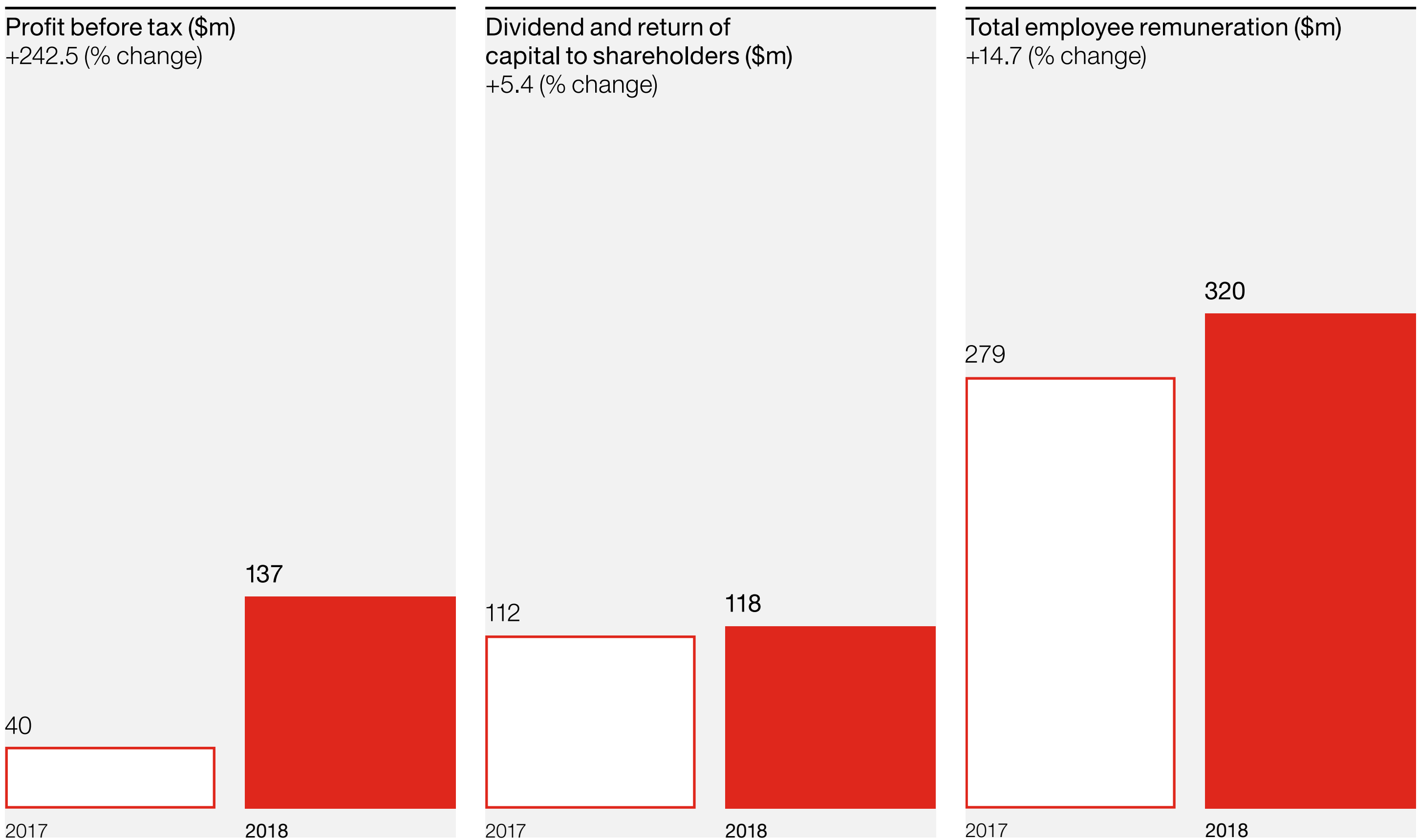
The table below shows the percentage change in base salary, benefits and annual bonus of the Chief Executive between the 2017 and 2018 financial years. As the Chief Executive is based in the UK, UK-based employees have been used as the comparator group for base salary – this ensures that any comparison takes into account inflation and country-specific benefits package. For the bonus, we have used Group employees as the comparator. The percentage change is based on employees who were employed and eligible for a salary review and bonus in both financial years.

	% change 2017 to 2018		% change 2016 to 2017	
	CEO	Employee	CEO	Employee
Base salary	3.4	3.0	2.5	3.0
Benefits (including retirement benefits)	3.3	2.7	3.4	8.0
Bonus	N/A*	56.5	(100.0)	(77.8)

*No bonus was paid to the CEO in respect of 2017.

Relative importance of the spend on pay

The charts below show the relative movement in profit, shareholder returns and employee remuneration for the 2018 and 2017 financial years. Shareholder return for the year incorporates the distribution made in respect of that year. Employee remuneration includes salary, benefits, bonus, long-term incentives and retirement benefits. Profit is the ultimate driver behind the performance metrics of the bonus and long-term incentive schemes. Profit before tax can be located on page 104.



Remuneration for the wider workforce

The Remuneration Committee receives regular information on Group-wide remuneration policies and uses internal and external measures to assess the appropriateness of remuneration including gender analysis and market benchmarking of pay, bonus pools split by business area, levels of share plan participation and pay ratios between Executives and average employees. The Committee will continue to monitor market practice in this area, given this is an area of particular shareholder focus and also in light of the provisions detailed within the revised UK Corporate Governance Code.

Although the Company is not technically subject to the UK disclosure requirements relating to the disclosure of CEO pay ratios which come into effect next year, we have voluntarily opted to provide information this year.

By design, the remuneration of our most senior executives, including the CEO, is more highly performance geared than other roles in the business. The Board therefore appreciates that the ratio between the pay of the CEO and wider employees can vary significantly over time. For example, in a year when the business performs well, the ratio would typically be higher. In contrast, if the CEO's incentives lapse in full, the ratio will be lower.

The CEO's latest single figure total remuneration compared with the median (50th percentile) remuneration of the Company's UK employees is shown below, along with the 25th and 75th percentiles.

	CEO pay ratio
75th percentile	1:15
50th percentile	1:30
25th percentile	1:36

For simplicity, the employees at 25th, 50th and 75th percentiles were identified using the latest gender pay gap information. The Company intends to keep the methodology under review in future years.

Payments for loss of office and payments to past Directors

There were no payments made for loss of office or payments to past Directors during 2018.

Implementation of remuneration policy for 2019

Salary

Annual salary reviews take effect from April each year. For 2019, salaries for Executive Directors will be increased by 2.7% in line with other UK-based employees.

Salaries from April 2019 will be as follows:

	April 2019 £
Bronek Masojada	636,500
Richard Watson	490,000
Aki Hussain	490,000

Annual bonus

The maximum opportunity and overall bonus structure for the year ending 31 December 2019 will remain unchanged.

In determining the size of the Executive Director bonuses, the Committee uses the ranges below to support its decision-making process. These ranges enable the Remuneration Committee to award payments based on the achievement of specific objectives (not prospectively disclosed as commercially sensitive) and the context in which performance has been delivered.

Individual bonuses are based on the results of the business area, individual performance and the size of the relevant bonus pool. In determining the bonuses to be paid to Executive Directors, the Committee bases its judgements on both the performance of the Group and a robust assessment of individual performance.

Pre-tax return on equity	Indicative bonus range (% of max)
Less than RFR* +<5%	Nil
RFR +5% to RFR +12.5%	0-15%
RFR +10% to RFR +17.5%	15-40%
RFR +15% to RFR +22.5%	30-60%
RFR +20% to RFR +25%	50-70%
Greater than RFR +22.5%	60-100%

*Risk-free rate.

The risk-free rate for 2019 will be 1.5%.

Long-term incentives

The maximum opportunity and overall PSP structure for 2019 will remain unchanged. For 2019, Performance Share Plan awards will continue to be measured against growth in net asset value (NAV) plus dividends, measured on a per share basis. The Committee deems growth in NAV to be the most appropriate metric for the PSP given that our strategy is built around the objective of generating long-term shareholder value and NAV is aligned with shareholder value creation.

	Growth in net asset value plus dividend measured on a per share basis %	Proportion of PSP vesting %
Minimum threshold vesting	RFR + 6 = 7.5	20
Maximum vesting	RFR + 14 = 15.5	100
Straight-line vesting between these points		

The maximum opportunity for all Executive Directors will be 200% of salary. The risk-free rate (RFR) will be 1.5% for 2019.

Membership of the Remuneration Committee

The Committee members at 31 December 2018 were Caroline Foulger, Robert McMillan, Lynn Pike, Anne MacDonald, Thomas Hürlimann, Michael Goodwin, Constantinos Miranthis and Colin Keogh (Chairman). No Director or Committee member was involved in determining their own remuneration during the year.

Remuneration Committee fees

Non Executive Director fees were reviewed in December 2018. No amendments are proposed for 2019.

External advisors

The Committee received independent advice from Deloitte, an independent firm of remuneration consultants appointed by the Committee in 2013, following a competitive tender process. Deloitte is a founder member of the Remuneration Consultants Group and, as such, voluntarily operates under its code of conduct. During the year, Deloitte's executive compensation advisory practice advised the Committee on developments in market practice, corporate governance and institutional investor views, and on the development of the Company's incentive arrangements. Total fees for advice provided to the Committee during the year were £27,500 based on a time and materials basis. The Committee regularly reviews the advice it receives and is satisfied that this has been objective and independent. During the year Deloitte also provided the Company with other tax and consulting services.

In addition to the external advisors, the Group HR Director provided material assistance to the Remuneration Committee during the year.

Statement of shareholder voting

At the AGM on 17 May 2018, the Directors' annual report on remuneration received the following votes from shareholders:

	Remuneration policy	Annual report on remuneration
For	177,072,418	224,879,428
%	84.46%	98.29%
Against	32,579,285	3,919,130
%	15.54%	1.71%
Withheld	1,016,024	587,915
Total votes	210,667,727	229,386,473

The remuneration policy was last voted on at the 2017 AGM.

Remuneration policy

Hiscox has a forward-looking remuneration policy for its Board members. Shown below is the updated policy including changes made to be implemented from 1 January 2018. These amendments are shown in italics. The policy was last approved at the 2017 AGM and the original policy can be viewed in the 2016 Annual Report and Accounts at www.hiscoxgroup.com.

Future policy table

Executive Director remuneration

Base salary

Purpose and link to strategy	Fixed pay elements enable the Company to be competitive in the recruitment market when looking to employ individuals of the calibre required by the business.
Operation	Base salary is normally reviewed annually, taking into account a range of factors including inflation rate movements by country, relevant market data and the competitive position of Hiscox salaries by role. Individual salaries are set by taking into account the above information as well as the individual's experience, performance and skills, increases to salary levels across the wider Group and overall business performance. By exception, an individual's salary may be amended outside of the annual review process.
Maximum potential value	The salaries for current Executive Directors are set out on page 72. Executive Directors' salary increases will normally be in line with overall employee salary increases in the relevant location. Increases above this level may be considered in other circumstances as appropriate (for example, to address market competitiveness, development in the role, or a change in role size, scope or responsibility).
Performance metrics	Individual and business performance are taken into account when setting salary levels.
Application to broader employee population	Process for review of salaries is consistent for all employees.

Future policy table
Executive Director remuneration

Benefits (including retirement benefits)

Purpose and link to strategy	Employee benefits enable the Company to be competitive in the recruitment market when looking to employ individuals of the calibre required by the business.
Operation	**Retirement benefits** These vary by local country practice but all open Hiscox retirement schemes are based on defined contributions or an equivalent cash allowance. This approach will be generally maintained for any new appointments other than in specific scenarios (for example, local market practice dictates other terms). For current Executive Directors, a cash allowance of up to 10% of salary is paid in lieu of the standard employer pension contribution. Certain Board members retain legacy interests in closed defined benefit schemes. However, there is no entitlement to any further accrual under these plans. **Other benefits** Benefits are set within agreed principles but reflect normal practice for each country. Hiscox benefits include, but are not limited to: health insurance, life insurance, long-term disability schemes and participation in all-employee share plans such as the Sharesave Scheme. For new hires and changes in role, the Committee may provide reasonable additional benefits based on the circumstances (for example, travel allowance and relocation expenses).
Maximum potential value	Set at an appropriate level by reference to the local market practice and reflecting individual and family circumstances.
Performance metrics	None.
Application to broader employee population	Executive Directors' benefits are determined on a basis consistent with all employees.

Future policy table
Executive Director remuneration

Annual bonus

Purpose and link to strategy	To reward for performance against key objectives and achievement of financial results over the financial year. To provide a direct link between reward and performance. To provide competitive compensation packages.
Operation	Executive Directors participate in profit-related bonus pools. Bonus pools are calculated at a business unit level and for the Group as a whole on the basis of Group financial results. For 2018, the bonus pool will be funded by a set percentage of profits on achievement of a hurdle rate of ROE. The bonus for prior years was determined on a similar basis. Further detail is set out on page 73. For Executive Directors, individual allocations from the pool are determined by the Remuneration Committee based on a judgement of various factors including: — size of the Group bonus pool; — results of business area (where relevant); — individual performance. Amounts are paid in accordance with the bonus deferral mechanism described opposite. Bonus awards are non-pensionable. Bonus awards are subject to malus and clawback provisions as described in the notes to the policy table on page 90.
Maximum potential value	The maximum bonus opportunity for the Executive Directors will be as follows: — CEO and CFO – 400% of salary; — CUO – up to 500% of salary. The Company has a robust track record of paying bonuses which are proportionate to financial results, see page 74 of this report for further details. Where performance is deemed to be below a predetermined hurdle, payouts will be nil. The total of individual bonuses paid to Executive Directors for a year will not normally exceed 15% of the total pool. If the number of Executive Directors increased in the future, this percentage would be adjusted as required.
Performance metrics	Performance is measured over one financial year. Bonus pools are determined based on financial performance, therefore this is the main determinant of overall bonus payouts. A hurdle of financial performance is set annually. Performance above this hurdle is rewarded and where performance falls below this hurdle, payouts will be nil.
Application to broader employee population	The operation of the annual incentive is consistent for the majority of employees across the Group. Arrangements tailored to roles and responsibilities are operated for selected positions. Bonuses for more junior employees are calculated using a more formulaic approach. Further details are set out on page 73.

Future policy table
Executive Director remuneration

Bonus deferral

Purpose and link to strategy	To encourage retention of employees. To facilitate and encourage share ownership in order to align senior employees with Hiscox shareholders.
Operation	Larger bonuses are normally deferred over a three-year period and paid subject to continuing service as explained in the table below. Deferral points are determined based on the currency in which the Executive Director's salary is paid and are normally as follows:

Bonus of £50,000, €75,000, $100,000, and below	Paid shortly after the end of the financial year in which the bonus was achieved.
Bonus above £50,000 and below £100,000 Bonus above €75,000 and below €150,000 Bonus above $100,000 and below $200,000	£50,000, €75,000, $100,000, paid shortly after the end of the financial year in which the bonus was achieved. Balance of bonus split 50% to be paid after year two (24 months after the start of the bonus year), and 50% after year three (36 months after the start of the bonus year).
Bonus above £100,000, €150,000, $200,000	50% of bonus paid shortly after the end of the financial year. Balance of bonus split 50% to be paid after year two, and 50% after year three.

Participants are able to (subject to any local tax/legal/regulatory restrictions) draw deferred bonuses early in certain circumstances in order to enable the acquisition of Hiscox shares. Such amounts remain subject to continued employment.

The Remuneration Committee can agree to early payment of deferred bonuses to Executive Directors on an exceptional basis at their discretion.

Deferred awards are subject to malus and clawback provisions as described in the notes to the policy table on page 90.

Maximum potential value	N/A.
Performance metrics	N/A.
Application to broader employee population	Approach is consistent for all employees across the Group who are awarded a sizeable bonus.

Future policy table
Executive Director remuneration

Performance Share Plan (PSP)

Purpose and link to strategy	To motivate and reward for the delivery of long-term objectives in line with business strategy. To encourage share ownership among participants and align interests with shareholders. To provide competitive compensation packages for senior employees.
Operation	Awards are granted under the PSP approved by shareholders in 2016 (with previous awards granted under the equivalent plan implemented in 2006). All awards are governed by the rules of the relevant plan under which they are granted. Share awards (typically structured as either conditional awards or nil cost options) are made at the discretion of the Remuneration Committee. Awards normally vest after a three-year period subject to the achievement of performance conditions. An additional holding period, which is currently two years, may also apply. Awards are generally subject to continued employment, however awards may vest to leavers in certain scenarios (for example, 'good' leaver circumstances). Dividends (or equivalents) may accrue on vested shares prior to release. Awards are subject to malus and clawback provisions as described in the notes to the policy table on page 90.
Maximum potential value	Maximum annual grant of up to 200% of salary in respect of any one financial year.
Performance metrics	The performance conditions for awards are set to align with the long-term objectives of the Company. The Committee reviews the targets prior to each grant to ensure that they remain appropriate. Currently, the performance measures are linked to the achievement of ROE performance over an agreed hurdle, during the performance period. *The minimum threshold vesting will be 20% rather than 25% for PSP awards granted from 2018 onwards.* For delivery of the threshold hurdle, up to 25% of the relevant award will vest. For full vesting, the stretch hurdle needs to be met in full. Usually, there will be straight-line vesting for performance between the threshold and stretch hurdle. *The minimum threshold vesting will be 20%, rather than 25%, for PSP awards granted from 2018 onwards.* Where the Committee considers it appropriate to do so, under the plan rules the Committee is able to modify performance criteria for outstanding awards on the occurrence of certain events (for example, major disposal).
Application to broader employee population	Participation in this plan is restricted to Executive Directors and other senior individuals.

Future policy table
Executive Director remuneration

Shareholding guidelines

Purpose and link to strategy	To ensure Executive Directors are aligned with shareholder interests.
Operation	Within five years of becoming an Executive Director, individuals will normally be expected to own Hiscox shares valued at 150% of salary. *From 2018 this increased to 200%.*
Maximum potential value	N/A.
Performance metrics	N/A.
Application to broader employee population	Executive Directors are required to hold more shares than other senior managers.

Future policy table
Non Executive Director remuneration

General approach	The total aggregate fees payable are set within the limit specified by the Company's Bye-laws. The fees paid are determined by reference to the skills and experience required by the Company as well as the time commitment associated with the role. The decision-making process is informed by appropriate market data. Non Executive Directors are not eligible for participation in the Company's incentive plans. Travel and other reasonable expenses incurred in the course of performing their duties are reimbursed to Non Executive Directors. Non Executive Directors are included on the directors and officers' indemnity insurance. The current fees payable to Non Executive Directors are set out on page 77.
Chairman	The Chairman typically receives an all-inclusive fee in respect of the role. In addition to his fees the Chairman may be provided with incidental benefits (for example, private healthcare and life assurance). The remuneration of the Chairman is determined by the Committee.
Non Executive Directors	Non Executive Directors receive an annual fee in respect of their Board appointments together with additional compensation for further duties (for example, Board Committee membership and chairmanship). The fees for the Non Executive Directors (excluding the Chairman) are determined by the Chairman.

The performance targets for the annual bonus and share plan awards to Executive Directors are intended to be closely aligned with the Company's short-term and long-term objectives.

Performance measure targets and target setting

Notes to the policy table

Performance measure targets and target setting

The performance targets for the annual bonus and share plan awards to Executive Directors are intended to be closely aligned with the Company's short-term and long-term objectives. The intention is to provide a direct link between reward levels and performance.

The Company operates a bonus pool approach for the annual incentive. This ensures that both individual bonus levels and overall spend are commensurate with the performance of the Company. The Committee applies judgement based on a range of factors (as described in the table on pages 84 to 89) to ensure that outcomes for Executive Directors are based on performance in-the-round rather than on a formulaic outcome. The profit pool approach currently used ensures that overall bonus amounts are aligned to the performance of the Company and remain appropriate and affordable.

The Performance Share Plan (PSP) performance measures are intended to motivate and reward to deliver long-term Company success. The Committee considers performance metrics and targets prior to the grant of each to ensure that these remain suitable and relevant.

Detailed provisions

The Committee may make minor changes to this remuneration policy to aid in its operation or implementation without seeking shareholder approval (for example, for regulatory or administrative purposes), provided that any such change is not to the material advantage of Directors. For the avoidance of doubt the Committee may continue to operate the share awards under the 2006 and 2016 PSP in accordance with the rules (for example, the treatment of awards in the context of a change of control or other forms of corporate restructure).

The Committee may continue to satisfy remuneration payments and payments for loss of office (including the exercise of any discretions available to the Committee in connection with such payments) where the terms of the payment were: i) agreed before 15 May 2014 when the first approved remuneration policy came into effect; ii) agreed before the policy set out above came into effect, provided that the terms of the payment were consistent with the shareholder-approved Directors' remuneration policy in force at the time they were agreed; or iii) agreed at a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, the payment was not in consideration for the individual becoming a Director of the Company. For these purposes, such payments include the Committee satisfying awards of variable remuneration.

Malus and clawback provisions

In respect of unvested compensation, specifically deferred bonuses and unvested PSP awards, the Committee may, in its absolute discretion, determine at any time prior to the vesting of an award to reduce, cancel or impose further conditions in the following circumstances:

- a retrospective material restatement of the audited financial results of the Group for a prior period error in accordance with IAS 8;
- actions of gross misconduct, including fraud, by the participant or their team leading to the Company suffering significant reputational or financial damage.

For awards granted in respect of 2015 and future years, in the circumstances described above, annual bonus and PSP awards granted to Executive Directors shall also be subject to clawback provisions for up to two years after the end of the relevant performance period.

Recruitment policy

A new hire will ordinarily be remunerated in accordance with the policy described in the table on the previous pages. In order to define the remuneration for an incoming Executive Director, the Committee will take account of:

- prevailing competitive pay levels for the role;
- experience and skills of the candidate;
- awards (shares or earned bonuses) and other elements which will be forfeited by the candidate;
- transition implications on initial appointment.

The Committee will always aim to provide a remuneration package which is consistent with the overall Hiscox approach.

A 'buy-out' payment/award may be necessary in respect of arrangements forfeited on joining the Company. The size and structure of any such buy-out arrangement will take account of relevant factors in respect of the forfeited terms

including potential value, time horizons and any performance conditions which apply. The objective of the Committee will be to suitably limit any buy-out to the commercial value forfeited by the individual.

On initial appointment (including interim Director appointments) the maximum level of variable remuneration (excluding any buy-outs) is capped at the maximum level set out in the policy table on pages 84 to 89. Within these limits and where appropriate the Committee may tailor the award (for example, time frame, form, performance criteria) based on the commercial circumstances. Shareholders would be informed of the terms for any such arrangements. Ordinarily, it would be expected that the package on recruitment would be consistent with the usual ongoing Hiscox incentive arrangements.

On the appointment of a new Non Executive Chairman or Non Executive Director, the fees will normally be consistent with the policy. Fees to Non Executives will not include share options or other performance-related elements.

Service contracts

It is the Company's policy that Executive Directors should have service contracts with an indefinite term which can be terminated by the Company by giving notice not exceeding 12 months or the Director by giving notice of six months. Non Executive Directors are appointed for a three-year term, which is renewable, with three months' notice on either side, no contractual termination payments being due and subject to retirement pursuant to the Bye-laws at the Annual General Meeting. The contract for the Chairman is subject to a six-month notice provision on either side.

Policy on payment for loss of office

Subject to the execution of an appropriate general release of claims an Executive Director may receive on termination of employment by the Company:

1. Notice period of up to 12 months

Executive to remain on the payroll but may be placed on gardening leave for the duration of the notice period (or until they leave early by mutual agreement, whichever is sooner). During this period they will be paid as normal, including base pay, pension contributions (or cash allowance as appropriate) and other benefits (for example, healthcare).

2. Bonus payment for the financial year of exit

The Committee may pay a bonus calculated in line with the normal bonus scheme timings and performance metrics. The bonus amount would normally be pro-rated depending on the proportion of the financial year which has been completed by the time of the termination date.

3. Release of any deferred bonuses

All outstanding bonuses deferred from the annual incentive scheme will normally be paid in full.

4. Unvested Performance Share Plan awards

Treatment would be in accordance with the plan rules and relevant grant documentation. The intended approach is summarised below.

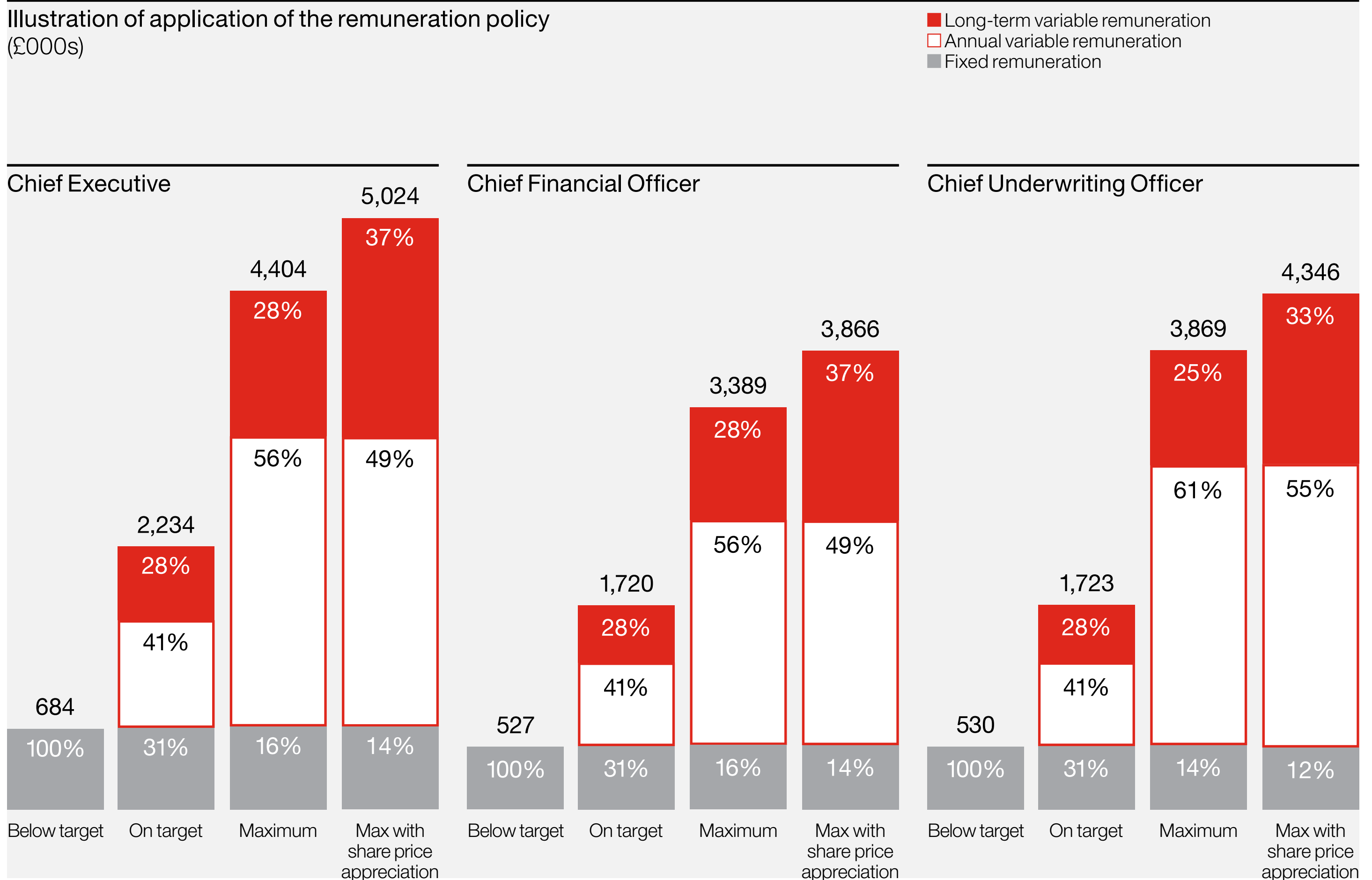
- Awards will vest in line with the normal scheme vesting date (unless the Committee determines otherwise). Awards vest to the extent that the relevant performance target is considered to have been met.
- The award will normally be pro-rated to reflect the period which has elapsed from the commencement of the award to the date of termination unless the Committee determines otherwise.

If the departing Executive Director does not sign a release of claims, they would normally be entitled to payments defined under point 1 only. In the event that the Executive is dismissed for gross misconduct, they would forfeit any payments under UK and Bermudian employment law. In the event of a voluntary resignation to join another company, no payments would normally be made other than remaining on the payroll, with associated benefits, during the contractual notice period of six months.

Consideration of shareholder views

Hiscox regularly discusses remuneration policy matters with a selection of shareholders. The Remuneration Committee takes into consideration the range of views expressed in making its decisions.

Through conversations with shareholders during the 2017 AGM season, some themes emerged on how we could improve our approach and the Committee made a number of changes to how the policy was implemented from 2018 onwards.



The charts above have been compiled using the following assumptions.

Fixed remuneration	Fixed reward (base salary, benefits and retirement benefit). — Salary with effect from 1 April 2018. — Benefits as received during 2018, as disclosed in the Executive Director remuneration table on page 72. — Retirement benefit as received during 2018, as disclosed in the Executive Director remuneration table on page 72.
Variable remuneration	Assumptions have been made in respect of the annual incentive and the PSP for the purpose of these illustrations. — Annual incentive: the amounts shown in the scenarios are for illustration only. In practice, the award would be determined based on a range of performance factors and therefore vary depending on the circumstances. The maximum award reflects the incentive caps described at the beginning of this report. — PSP: scenario analysis assumes awards are granted at the maximum level set out in the policy table on page 88. In practice, award levels are determined annually and are not necessarily granted at the plan maximum every year.

Performance scenarios	
Below target performance	Fixed reward only.
On target performance	Fixed reward plus variable pay for the purpose of illustration as follows. — Annual incentive: assume a bonus equivalent to 150% of salary. — PSP: assumes vesting of 50% of the maximum award.
Maximum performance	Fixed reward plus variable pay for the purpose of illustration as follows. — Annual incentive: maximum bonus equivalent to 400% of salary for the CEO and CFO and 500% of salary for the CUO. — PSP: assumes vesting of 100% of the maximum award.
Maximum performance with share price appreciation	Fixed reward plus variable pay for the purpose of illustration as follows. — Annual incentive: maximum basis equivalent to 400% of salary for the CEO and CFO and 500% of salary for the CUO. — PSP: assumes vesting of 100% of the maximum award plus assumed share price growth of 50%.

Directors' report

The Directors have pleasure in submitting their Annual Report and consolidated financial statements for the year ended 31 December 2018.

Management report
The Company is a holding company for subsidiaries involved in the business of insurance and reinsurance in Bermuda, the USA, the UK, Guernsey, Europe and Asia. The information found on pages 10 to 17, 42 to 51 and 104 to 160 fulfils the requirements of the management report as referred to in Chapter 4 of the Disclosure Guidance and Transparency Rules (DTR). This includes additional explanation of the figures detailed in the financial statements and the office locations of the Group in different countries.

The key performance indicators are shown on page 2. Details of the use of financial instruments are set out in note 19 to the consolidated financial statements. An analysis of the development and performance of the business during the financial year, its position at the end of the year, any important events since the end of the year and the likely future development can be found within the Chief Executive's report on pages 10 to 17. The Chief Executive's report also describes the main trends and factors likely to affect the future development, performance and position of the Company's business and includes a description of the Company's strategy and business model. The Company's strategy is also described on page 3. A description of the principal risks and uncertainties and how they are managed or mitigated can be found in the risk management section on pages 42 to 51. In addition, note 3 to the consolidated financial statements provides a detailed explanation of the principal risks which are inherent to the Group's business and how those risks are managed.

The confirmation required by C.2.1 of the UK Corporate Governance Code can be found on page 63.

Corporate governance statement
The information that fulfils the requirements of the corporate governance statement as referred to in DTR 7.2 can be found on pages 61 to 64 in this report.

Diversity
The composition of the Board is described on pages 58 and 59. The percentage of persons of each gender who were i) Hiscox Partners and ii) employees of the Hiscox Group, excluding the Board, is set out in the table to the right. Hiscox's approach to diversity and inclusion is outlined on page 56.

Financial results
The Group achieved a pre-tax profit for the year of $137.4 million (2017: $39.7 million). Detailed results for the year are shown in the consolidated income statement on page 104, and also within the Group financial performance section on pages 24 to 25.

Going concern
A review of the financial performance of the Group is set out on pages 24 to 25. The financial position of the Group, its cash flows and borrowing facilities are included therein. The Group has considerable financial resources and a well-balanced book of business.

After making enquiries, the Directors have an expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future, a period of at least 12 months from the date of this report. For this reason they continue to adopt the going concern basis in preparing the consolidated financial statements.

Viability
The statement required to be included in the Annual Report under C.2.2 of the UK

Diversity

	Male %	Female %
Hiscox Partners*	77.8	22.2
Employees	49.9	50.1

*Hiscox Partner is an honorary title given to employees who make significant contributions to the development and profitability of the Group. The Partnership encourages a proprietorial attitude, and up to 5% of the total workforce are Hiscox Partners.

41.85¢

Total dividend payment for the year ended 31 December 2018.

Major interests in shares
As at the year end, the Company had been notified of the following interests of 5% or more of voting rights in its ordinary shares:

	Number of shares	% of issued share capital as at 31 December 2018*
Invesco Limited[1]	17,211,598	6.19
Massachusetts Financial Services Company[1]	36,386,481	13.08
FMR LLC[1]	22,167,818	7.97
BlackRock, Inc.[1,2]	22,195,030	8.13

*Per RNS announcement there were 287,792,195 shares in issue (excluding Treasury shares) as at 31 December 2018.
[1]Indirect holdings.
[2]Notified on 29 January 2018.

As at 22 February 2019, no changes have been notified to the Company.

Corporate Governance Code can be found on page 64.

Dividends
An interim dividend of 13.25¢ was paid on 11 September 2018 in respect of the year ended 31 December 2018. As in previous years a scrip dividend alternative was offered. The Directors are proposing payment of a final dividend in respect of the year ended 31 December 2018 of 28.6¢ which will be paid on 12 June 2019 to shareholders on the register at 10 May 2019.

Bye-laws
The Company's Bye-laws contain no specific provisions relating to their amendment and any such amendments are governed by Bermuda Company Law and subject to the approval of shareholders in a general meeting. A copy of the Company's Bye-laws is available for inspection at the Company's registered office.

Share capital
Details of the structure of the Company's share capital and changes in the share capital during the year are disclosed in note 22 to the consolidated financial statements. The ordinary shares of 6.5p each are the only class of shares presently in issue and carry voting rights. There is power under Bye-law 45 of the Company's Bye-laws for voting rights to be suspended if calls on shares are unpaid. However, there are no nil or partly paid shares in issue on which calls could be made. The Bye-laws also allow the Company to investigate interests in its shares and apply restrictions including suspending voting rights where information is not provided. No such restrictions are presently in place. The Company was authorised by shareholders at the 2018 Annual General Meeting to purchase in the market up to 10% of the Company's issued ordinary shares. No shares have been bought back under this authority as at the date of this report.

Directors
The names and details of all Directors of the Company who served during the year and up to the date of this report are set out on pages 58 and 59. Details of the Chairman's professional commitments are included in his biography on page 58 and there were no changes during the year. The Bye-laws of the Company govern the appointment and replacement of Directors. In accordance with the UK Corporate Governance Code, all Directors will submit themselves for re-appointment at the Annual General Meeting.

Biographical details of the Directors are set out on pages 58 and 59 and the reasons why the Board believes they should be appointed or re-appointed will be set out in the circular which will accompany the notice of Annual General Meeting.

Political and charitable contributions
The Group made no political contributions during the year (2017: $nil). Information concerning the Group's charitable activities is contained in the responsibility section on pages 52 to 57.

Major interests in shares
As at the year end, the Company had been notified of the interests of 5% or more of voting rights in its ordinary shares outlined in the table above.

Any acquisitions or disposals of major shareholdings notified to the Company in accordance with DTR 5.1 are announced and those announcements are available on the Company's website, www.hiscoxgroup.com.

Power of Directors
The powers given to the Directors are contained in the Company's Bye-laws and are subject to relevant legislation and, in certain circumstances (including in relation to the issuing and buying back by the Company of its shares), approval by shareholders in a general meeting. At the Annual General Meeting in 2018, the Directors were granted authorities to allot and issue shares and to make market purchases of shares and intend to seek renewal of these authorities in 2019.

Disclosure under LR 9.8.4
The information that fulfils the reporting requirements relating to the following matters can be found at the pages identified below.

Details of long-term incentive schemes	Annual report on remuneration (page 83)
Allotment of shares for cash pursuant to employee share schemes	Note 22 to the consolidated financial statements on employee share schemes (page 143)

Annual General Meeting
The notice of the Annual General Meeting, to be held on 16 May 2019, will be contained in a separate circular to be sent to shareholders. The deadline for submission of proxies is 48 hours before the meeting.

By order of the Board
Marc Wetherhill
Secretary

Wessex House
45 Reid Street
Hamilton HM 12
Bermuda
25 February 2019

Directors' responsibilities statement

Directors' responsibilities statement

The Board is responsible for ensuring the maintenance of proper accounting records which disclose with reasonable accuracy the financial position of the Group. It is required to ensure that the financial statements present a fair view for each financial period. The Directors explain in the Annual Report their responsibility for preparing the Annual Report and Accounts.

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union, give a true and fair view, in all material respects, the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the management report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The Directors responsible for authorising the responsibility statement on behalf of the Board are the Chairman, Robert Childs, and the Chief Financial Officer, Hamayou Akbar Hussain.
The statements were approved for issue on 25 February 2019.

The Directors consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's and the Group's position and performance, business model and strategy.

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Financial summary

Independent auditor's report to the Board of Directors and the Shareholders of Hiscox Ltd

Report on the audit of the consolidated financial statements

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Hiscox Ltd (the Company) and its subsidiaries (together 'the Group') as at 31 December 2018, and their consolidated financial performance and their consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

What we have audited

Hiscox Ltd's consolidated financial statements comprise:

- the consolidated income statement for the year ended 31 December 2018;
- the consolidated statement of comprehensive income for the year ended 31 December 2018;
- the consolidated balance sheet as at 31 December 2018;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the 'Auditor's responsibilities for the audit of the consolidated financial statements' section of our report.

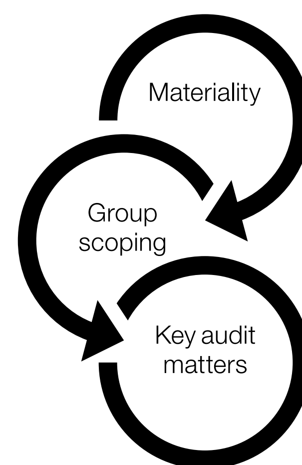
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Chartered Professional Accountants of Bermuda Rules of Professional Conduct (CPA Bermuda Rules) that are relevant to our audit of the consolidated financial statements in Bermuda. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the CPA Bermuda Rules.

Our audit approach

Overview



- Overall Group materiality: $27.7 million, which represents 0.75% of the gross earned premium for the year ended 31 December 2018.

- We performed full scope audit procedures over five individually financially significant components.
- For other components, we scoped the audit of these by performing audits over specified financial statement line item balances.
- For the remaining components that were not inconsequential, analytical procedures were performed by the Group engagement team.

- Valuation of incurred but not reported (IBNR) loss reserves and the associated reinsurers' share of IBNR loss reserves.
- Change in functional currency of certain trading subsidiaries and Hiscox Ltd's presentation currency.

Audit scope

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including, among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group materiality for the consolidated financial statements as a whole as set out in the table to the right. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate, on the consolidated financial statements as a whole.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above $1.4 million, as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Overall Group materiality	$27.7 million
How we determined it	0.75% of gross earned premium
Rationale for the materiality benchmark applied	In determining our materiality, we have considered financial metrics which we believe to be relevant to the primary users of the consolidated financial statements. We concluded gross earned premium was the most relevant benchmark to these users. Gross earned premium provides a good representation of the size and complexity of the business and it is not distorted by insured catastrophe events to which the Group is exposed or the levels of external reinsurance purchased by the Group.

Key audit matters
Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the key audit matter
Valuation of incurred but not reported (IBNR) loss reserves and the associated reinsurers' share of IBNR loss reserves. **Refer to notes 2.13 (b) and 23 to the consolidated financial statements for disclosures of related accounting policies and balances.** Total gross IBNR loss reserves and the associated reinsurers' share of IBNR loss reserves are material estimates in the consolidated financial statements and as at 31 December 2018 amount to $3.035 billion and $1.357 billion respectively. The methodologies and assumptions used to develop IBNR loss reserves and the reinsurers' share of IBNR loss reserves involves a significant degree of judgement. As a result, we focused on this area as the valuation can be materially impacted by numerous factors including: — the underlying volatility attached to estimates for certain classes of business, where small changes in assumptions can lead to large changes in the levels of the estimate held and the reported profit; — the risk of inappropriate assumptions used in determining current year estimates. Given that limited data is available, especially for 'long-tailed' classes of business, there is greater reliance on expert judgement in management's estimation; — the judgements made in significant areas of uncertainty, for example, liability and casualty classes of business; and — the risk that IBNR loss reserve estimates in respect of natural catastrophes and other large claims losses are inappropriate. There is significant judgment involved in the estimation of such loss estimates, particularly as they are often estimated based on limited data.	We have understood, evaluated and tested the design and operational effectiveness of key controls in place in respect of the valuation of IBNR loss reserves and the associated reinsurers' share of IBNR loss reserves. This work, supplemented with tests of detail, included (i) reviewing and testing the reconciliation of data from the underlying policy administration systems to the data used in the actuarial projections, (ii) testing the completeness and accuracy of premiums and claims data used in the actuarial projections, and (iii) testing to ensure IBNR loss reserves, as a component of insurance liabilities, and the associated reinsurers' share of IBNR loss reserves were reviewed, approved and reconciled to the consolidated financial statements. In performing our detailed audit work over the valuation of IBNR loss reserves and the associated reinsurers' share of IBNR loss reserves we used PwC actuarial specialists. Our procedures included: — developing independent point estimates for classes of business considered to be higher risk, particularly focusing on the largest and most uncertain estimates, as at 30 September 2018 and performing roll-forward testing to 31 December 2018. For these classes, we compared our re-projected estimates to those booked by management; — testing, for the other classes of business, (including those impacted by natural catastrophes and other large claims), the methodology and assumptions used by management to derive the IBNR loss reserve estimates; — performing analytical review procedures over the remaining classes of business to evaluate IBNR loss reserves; and — re-calculating gross to net ratios on a test basis against the estimated IBNR loss reserves to calculate the estimated reinsurers' share of IBNR loss reserves. Based on the work performed we found that the IBNR loss reserves and the associated reinsurers' share of IBNR loss reserves were supported by the evidence we obtained.

Key audit matter	How our audit addressed the key audit matter
Change in functional currency of certain trading subsidiaries and Hiscox Ltd's presentation currency. **Refer to note 2.1 to the consolidated financial statements for related disclosures.** On 1 January 2018, the functional currency of a number of trading subsidiaries changed from Sterling to US Dollars. The change was as a result of changes made to various underlying contracts and arrangements (i.e. quota share contracts, profit commission and capital arrangements) which were effected on 1 January 2018 and are denominated in US Dollars as opposed to Sterling resulting in a significant proportion of earnings in US Dollars. Management elected to change the presentation currency at the Hiscox Ltd level as a result of the change in functional currency of these trading subsidiaries. We focused on these areas due to the pervasive impact on the consolidated financial statements, as well as the management judgements applied in the process.	Our work over the changes to the functional currency included the following: — we obtained management's analysis and results of their determination. We critically evaluated the underlying transactions of the trading subsidiaries for which management determined there was a change in functional currency. We considered the weighting of the various currencies that business is transacted in from a revenue and an expense perspective; — we compared management's conclusions to the applicable accounting standards; — we inspected and evaluated the underlying contracts to form our own conclusions over the operational currencies; and — we re-performed management's calculations to test that (i) all balance sheet financial statement line items had been converted to the new functional currency at the spot rate at the date of change, and (ii) from 1 January 2018 foreign currency income statement transactions were accurately translated to US Dollars including testing the system changes to maintain underlying US Dollar ledgers. We agreed the rates of exchange applied to an independent source. Our work over the change in presentation currency included the following: — We re-performed the conversion of the primary statements and notes for the prior financial year which was previously presented in Sterling. We agreed the conversion of all asset and liability items (and related notes) from Sterling to US Dollars at balance sheet closing rates and agreed the conversion of all income statement items (and related notes) from Sterling to US Dollars at average exchange rates for the period which we determined was a proxy for spot rates; — For equity items, we used audited financial statements to determine the dates of historic transactions. We re-calculated the conversion from Sterling to US Dollars at the spot rate of exchange on those dates; and — We agreed the rates of exchange utilised to an independent source. Based on the procedures performed, no adjustments to the financial statements or disclosures were deemed necessary and the judgements applied were appropriate in the circumstances.

How we tailored our Group audit scope
We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

Hiscox Ltd is the parent of a group of entities. The financial information of this Group is included in the consolidated financial statements of Hiscox Ltd. The Group is structured into four segments (see Note 4 to the consolidated financial statements) and is a consolidation of over 50 separate legal entities.

The Group is a global specialist insurer and reinsurer. The Group's operations primarily consist of the legal entity operations in the United Kingdom, Europe, the United States and Bermuda. A full scope audit was performed for five components located in the United Kingdom and Europe, the United States and Bermuda. Financial statement line item audit procedures were also performed over components in the United Kingdom and Bermuda. Taken together, this work gave us over 90% coverage of the Group's gross earned premium and over 85% of the Group's total assets.

The five full scope audit components are:
(i) Hiscox Dedicated Corporate Member Syndicate No. 33,
(ii) Hiscox Dedicated Corporate Member Syndicate No. 3624,
(iii) Hiscox Insurance Company Limited,
(iv) Hiscox Insurance Company Inc. and
(v) the parent company, Hiscox Ltd.

For other components, we identified certain account balances which were considered to be significant in size or audit risk at the financial statement line item level in relation to the Group's consolidated financial statements, and scoped the audit of these by performing financial statement line item audits over the specified balances. Analytical procedures over the remaining components that were not inconsequential were performed by the Group engagement team.

In establishing the overall approach to the Group audit, we determined the type of work that needed to be performed at the reporting units by us, as the Group engagement team, or component audit teams within the PwC United Kingdom, PwC United States and PwC Bermuda firms operating under our instruction. Where the work was performed by component audit teams, we determined the level of involvement we needed to have in the audit work at those reporting units to be able to conclude whether sufficient appropriate audit evidence had been obtained. The Group engagement team had regular interaction with the component teams, and senior engagement team members visited the United Kingdom, the United States and Bermuda during the audit process. Senior members of the Group engagement team reviewed all reports with regards to the audit approach and findings of the component auditors in detail. This together with additional procedures performed at the Group level, as described above, gave us the evidence we needed for our opinion on the Group's consolidated financial statements as a whole.

Other information
Management is responsible for the other information. The other information comprises the Annual Report (but does not include the consolidated financial statements and our auditor's report thereon).

Except as noted in the 'Report on other legal and regulatory requirements' section, our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements
Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements
Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:
- identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing

an opinion on the effectiveness of the Group's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management;
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

Going concern

The Directors have concluded that it is appropriate to adopt the going concern basis in preparing the consolidated financial statements, as explained on page 94. The going concern basis presumes that the Group has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the balance sheet date. As part of our audit we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Group's ability to continue as a going concern.

Directors' remuneration

The Company voluntarily prepares a report on Directors' remuneration in accordance with the provisions of the UK Companies Act 2006. The Directors have requested that we audit the part of the report on Directors' remuneration specified by the UK Companies Act 2006 to be audited as if the Company were a UK registered company.

In our opinion, the part of the report on Directors' remuneration to be audited has been properly prepared in accordance with the UK Companies Act 2006.

Corporate governance statement

Under the United Kingdom's Listing Rules we are required to review the part of the Corporate Governance Statement on pages 61 to 64 relating to eleven provisions of the UK Corporate Governance Code and the Directors have requested that we also review their statements on going concern and the longer-term viability of the Company as required for UK registered companies with a premium listing on the London Stock Exchange. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

The engagement partner on the audit resulting in this independent auditor's report is Arthur Wightman.

PricewaterhouseCoopers Ltd.
Chartered Professional Accountants
Hamilton, Bermuda
25 February 2019

Consolidated income statement

For the year ended 31 December 2018	Note	2018 Total $000	2017 Total (restated)* $000
Income			
Gross premiums written	4	3,778,341	3,286,021
Outward reinsurance premiums		(1,196,855)	(883,022)
Net premiums written	4	2,581,486	2,402,999
Gross premiums earned		3,699,802	3,295,965
Premiums ceded to reinsurers		(1,126,163)	(879,757)
Net premiums earned	4	2,573,639	2,416,208
Investment result	7	38,101	104,750
Other income	9	46,785	54,079
Total income		2,658,525	2,575,037
Expenses			
Claims and claim adjustment expenses	23.2	(2,326,632)	(2,489,598)
Reinsurance recoveries	23.2	1,100,803	1,178,682
Claims and claim adjustment expenses, net of reinsurance	23.2	(1,225,829)	(1,310,916)
Expenses for the acquisition of insurance contracts	15	(881,974)	(798,809)
Reinsurance commission income	15	240,303	210,879
Operational expenses	9	(605,718)	(528,973)
Net foreign exchange losses		(13,688)	(80,890)
Total expenses		(2,486,906)	(2,508,709)
Results of operating activities		171,619	66,328
Finance costs	10	(34,673)	(26,895)
Share of profit of associates after tax	14	429	259
Profit before tax		137,375	39,692
Tax expense	25	(9,376)	(5,788)
Profit for the year (all attributable to owners of the Company)		127,999	33,904
Earnings per share on profit attributable to owners of the Company			
Basic	28	45.1¢	12.0¢
Diluted	28	44.3¢	11.6¢

*See note 2.1 for further details.

Consolidated statement of comprehensive income

For the year ended 31 December 2018	2018 Total $000	2017 Total (restated)* $000
Profit for the year	127,999	33,904
Other comprehensive income		
Items that will not be reclassified to the income statement:		
Remeasurements of the net defined benefit obligation	20,249	11,173
Income tax effect	(4,135)	(2,279)
	16,114	8,894
Items that may be reclassified subsequently to the income statement:		
Exchange (losses)/gains on translating foreign operations	(17,906)	126,987
Income tax effect	–	–
	(17,906)	126,987
Other comprehensive income net of tax	(1,792)	135,881
Total comprehensive income for the year (all attributable to owners of the Company)	126,207	169,785

*See note 2.1 for further details.

The notes on pages 108 to 159 are an integral part of these consolidated financial statements.

Consolidated balance sheet

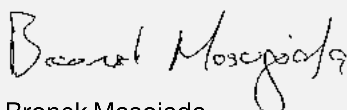
At 31 December 2018	Note	2018 $000	2017 (restated)* $000	2016 (restated)* $000
Assets				
Goodwill and intangible assets	12	**204,600**	186,038	153,418
Property, plant and equipment	13	**61,458**	65,628	60,047
Investments in associates	14	**9,922**	10,723	17,155
Deferred tax	26	**60,673**	53,462	51,326
Deferred acquisition costs	15	**455,857**	446,129	429,777
Financial assets carried at fair value	17	**5,029,681**	5,139,643	4,702,121
Reinsurance assets	16, 23	**2,456,575**	1,833,255	999,005
Loans and receivables including insurance receivables	18	**1,265,110**	1,121,452	995,592
Current tax asset		**13,578**	5,716	2,985
Cash and cash equivalents	21	**1,288,851**	867,767	824,373
Total assets		**10,846,305**	9,729,813	8,235,799
Equity and liabilities				
Shareholders' equity				
Share capital	22	**33,986**	33,913	33,806
Share premium	22	**57,680**	45,849	34,031
Contributed surplus	22	**183,969**	183,969	183,969
Currency translation reserve		**(328,488)**	(310,582)	(437,569)
Retained earnings		**2,368,897**	2,414,158	2,439,509
Equity attributable to owners of the Company		**2,316,044**	2,367,307	2,253,746
Non-controlling interest		**1,074**	1,074	1,074
Total equity		**2,317,118**	2,368,381	2,254,820
Employee retirement benefit obligations	27	**35,776**	64,114	69,612
Deferred tax	26	**–**	–	21,116
Insurance liabilities	23	**6,701,475**	6,007,750	4,777,693
Financial liabilities	17	**700,549**	391,110	342,604
Current tax		**10,307**	9,456	26,952
Trade and other payables	24	**1,081,080**	889,002	743,002
Total liabilities		**8,529,187**	7,361,432	5,980,979
Total equity and liabilities		**10,846,305**	9,729,813	8,235,799

*See note 2.1 for further details.

The notes on pages 108 to 159 are an integral part of these consolidated financial statements.

The consolidated financial statements were approved by the Board of Directors on 25 February 2019 and signed on its behalf by:

Aki Hussain
Chief Financial Officer



Bronek Masojada
Chief Executive Officer

Consolidated statement of changes in equity

	Note	Share capital $000	Share premium $000	Contributed surplus $000	Currency translation reserve $000	Retained earnings $000	Equity attributable to owners of the Company $000	Non-controlling interest $000	Total equity $000 (restated)*
Balance at 1 January 2017		33,806	34,031	183,969	(437,569)	2,439,509	2,253,746	1,074	2,254,820
Profit for the year (all attributable to owners of the Company)		–	–	–	–	33,904	33,904	–	33,904
Other comprehensive income net of tax (all attributable to owners of the Company)		–	–	–	126,987	8,894	135,881	–	135,881
Employee share options:									
Equity settled share-based payments		–	–	–	–	32,465	32,465	–	32,465
Proceeds from shares issued	22	77	6,084	–	–	–	6,161	–	6,161
Deferred and current tax on employee share options		–	–	–	–	6,832	6,832	–	6,832
Net movements of treasury shares held by Trust		–	–	–	–	(3,738)	(3,738)	–	(3,738)
Shares issued in relation to Scrip Dividend	22, 29	30	5,734	–	–	–	5,764	–	5,764
Dividends paid to owners of the Company	29	–	–	–	–	(103,708)	(103,708)	–	(103,708)
Balance at 31 December 2017		33,913	45,849	183,969	(310,582)	2,414,158	2,367,307	1,074	2,368,381
Profit for the year (all attributable to owners of the Company)		–	–	–	–	127,999	127,999	–	127,999
Other comprehensive income net of tax (all attributable to owners of the Company)		–	–	–	(17,906)	16,114	(1,792)	–	(1,792)
Employee share options:									
Equity settled share-based payments		–	–	–	–	(3,638)	(3,638)	–	(3,638)
Proceeds from shares issued	22	41	4,013	–	–	–	4,054	–	4,054
Deferred and current tax on employee share options		–	–	–	–	4,286	4,286	–	4,286
Net movements of treasury shares held by Trust		–	–	–	–	(76,474)	(76,474)	–	(76,474)
Shares issued in relation to Scrip Dividend	22, 29	32	7,818	–	–	–	7,850	–	7,850
Dividends paid to owners of the Company	29	–	–	–	–	(113,548)	(113,548)	–	(113,548)
Balance at 31 December 2018		**33,986**	**57,680**	**183,969**	**(328,488)**	**2,368,897**	**2,316,044**	**1,074**	**2,317,118**

*See note 2.1 for further details.

The notes on pages 108 to 159 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

For the year ended 31 December 2018	Note	2018 $000	2017 (restated)* $000
Profit before tax		137,375	39,692
Adjustments for:			
Net foreign exchange losses		13,688	80,890
Interest and equity dividend income		(102,955)	(81,590)
Interest expense		34,673	26,895
Net fair value losses/(gains) on financial assets		33,790	(34,360)
Depreciation, amortisation and impairment	9, 12, 13	33,184	27,908
Charges in respect of share-based payments	9, 22	(3,638)	32,465
Changes in operational assets and liabilities:			
Insurance and reinsurance contracts		136,338	326,046
Financial assets carried at fair value		2,978	(249,137)
Financial liabilities carried at fair value		(18,301)	18,022
Financial liabilities carried at amortised cost		(53,241)	30,430
Other assets and liabilities		56,721	(108,808)
Cash paid to the pension fund		(3,733)	–
Interest received		90,830	64,468
Equity dividends received		827	716
Interest paid		(33,876)	(25,664)
Current tax paid		(24,193)	(43,387)
Cash flows from subscriptions paid in advance		–	(9,339)
Net cash flows from operating activities		300,467	95,247
Proceeds from the sale of subsidiaries	14	–	18,696
Proceeds from the sale of associates	14	–	32,225
Purchase of property, plant and equipment		(7,832)	(9,074)
Purchase of intangible assets		(51,799)	(38,576)
Net cash flows from investing activities		(59,631)	3,271
Proceeds from the issue of ordinary shares†	22	4,054	6,161
Shares repurchased	22	(76,474)	(3,738)
Distributions made to owners of the Company†	22, 29	(105,698)	(97,944)
Proceeds from long-term debt issue, net of fees		380,265	–
Net cash flows from financing activities		202,147	(95,521)
Net increase in cash and cash equivalents		442,983	2,997
Cash and cash equivalents at 1 January		867,767	824,373
Net increase in cash and cash equivalents		442,983	2,997
Effect of exchange rate fluctuations on cash and cash equivalents		(21,899)	40,397
Cash and cash equivalents at 31 December	21	1,288,851	867,767

*See note 2.1 for further details.
†Following a review, prior year comparatives have been represented. Scrip dividend amounts of $5,764,000 are removed from these line items. This does not result in any change to net cash flows from financing activities.

The purchase, maturity and disposal of financial assets is part of the Group's insurance activities and is therefore classified as an operating cash flow. The purchase, maturity and disposal of derivative contracts is also classified as an operating cash flow.

Included within cash and cash equivalents held by the Group are balances totalling $211 million (2017: $178 million) not available for immediate use by the Group outside of the Lloyd's syndicate within which they are held. Additionally, $24 million (2017: $15 million) is pledged cash held against Funds at Lloyd's, and $10 million (2017: $7 million) held within trust funds against reinsurance arrangements.

The notes on pages 108 to 159 are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements

1 General information

The Hiscox Group, which is headquartered in Hamilton, Bermuda, comprises Hiscox Ltd (the parent company, referred to herein as the 'Company') and its subsidiaries (collectively, the 'Hiscox Group' or the 'Group'). For the period under review the Group provided insurance and reinsurance services to its clients worldwide. It has operations in Bermuda, the UK, Europe, Asia and the US with over 3,300 staff.

The Company is registered and domiciled in Bermuda and its ordinary shares are listed on the London Stock Exchange. The address of its registered office is: 4th Floor, Wessex House, 45 Reid Street, Hamilton HM 12, Bermuda.

2 Basis of preparation

The consolidated financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union, Section 4.1 of the Disclosure and Transparency Rules and the Listing Rules, both issued by the Financial Conduct Authority (FCA) and in accordance with the provisions of the Bermuda Companies Act 1981.

The consolidated financial statements have been prepared under the historical cost convention, except that pension scheme assets included in the measurement of the employee retirement benefit obligation which is determined using actuarial analysis, and certain financial instruments including derivative instruments, are measured at fair value.

In accordance with IFRS 4 Insurance Contracts, the Group continues to apply the existing accounting policies that were applied prior to the adoption of IFRS ('grandfathered') or the date of the acquisition of the entity. IFRS accounting for insurance contracts in UK companies was grandfathered at the date of transition to IFRS and determined in accordance with accounting principles generally accepted in the UK.

Items included in the financial statements of each of the Group's entities are measured in the currency of the primary economic environment in which that entity operates (the functional currency). The consolidated financial statements are presented in US Dollars and are rounded to the nearest thousand, unless otherwise stated.

The balance sheet of the Group is presented in order of increasing liquidity. All amounts presented in the income statements and statement of comprehensive income relate to continuing operations.

The financial statements were approved for issue by the Board of Directors on 25 February 2019.

2.1 Significant accounting policies

The principal accounting policies applied in the preparation of these consolidated Group financial statements are set out below. The most critical individual components of these financial statements that involve the highest degree of judgement or significant assumptions and estimations are identified in note 2.21.

Except as described below and overleaf, the accounting policies adopted are consistent with those of the previous financial year.

Changes in presentation currency and functional currency

With effect from 1 January 2018, the Group's presentation currency changed from Sterling to US Dollars, given that a significant majority of Group earnings are denominated in US Dollars. The Group believes that the presentation currency change will give investors and other stakeholders a clearer understanding of Hiscox's performance over time.

Following this change in accounting policy, the comparatives in the consolidated financial statements are represented in US Dollars using the procedures outlined below.

- Assets and liabilities are translated into US Dollars at closing rates of exchange. Trading results are translated into US Dollars at the rates of exchange prevailing at the dates of transaction or average rates where these are a suitable proxy. Differences resulting from the retranslation on the opening net assets and the results for the period have been presented in the currency translation reserve, a component within shareholders' equity.
- Share capital, share premiums and other reserves are translated at historic rates prevailing at the dates of transactions.
- The currency translation reserve was set to zero as of 1 January 2004, the transition date to IFRS. Cumulative currency translation adjustments are presented as if the Group had used US Dollars as the presentation currency of its consolidated financial statements since that date.

In addition, taking into consideration the following changes which were effective on 1 January 2018, the functional currency of Syndicate 33, Hiscox Dedicated Corporate Member Limited, Hiscox Syndicates Limited and Hiscox Capital Ltd changed from Sterling to US Dollars also effective from 1 January 2018.

- The denomination of a material internal quota share treaty has been changed from Sterling to US Dollars.
- The Syndicates' managing agent's profit commission and fee has been changed from Sterling to US Dollars.
- The Group has aligned its underwriting capital to US Dollars.

This change is accounted for prospectively from 1 January 2018.

New accounting standards, interpretations and amendments to published standards

A number of new standards, amendments to standards and interpretations, as adopted by the European Union, are effective for annual periods beginning on or after 1 January 2018. They have been applied in preparing these consolidated financial statements. There were no new standards, amendments or interpretations that had a material impact on the Group.

The new standards include:

- IFRS 15 *Revenue from Contracts with Customers* replaces IAS 18 and establishes principles for revenue recognition that apply to all contracts with customers except for insurance contracts, financial instruments and lease contracts. It requires an entity to recognise revenue when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. In particular, it specifies that variable consideration is only recognised to the extent that it is highly probable that a significant

2 Basis of preparation

2.1 Significant accounting policies

New accounting standards, interpretations and amendments to published standards continued

reversal will not occur. The adoption of this standard has an immaterial impact on the Group's financial statements, because the point at which control of a performance obligation is transferred to customers matches the point in which risk and rewards were transferred under IAS 18. Accounting policy 2.12 has been updated to reflect the new requirements.

The following new standards, and amendments to standards, are effective for annual periods beginning after 1 January 2018 and have not been applied in preparing these financial statements:

- IFRS 9 *Financial Instruments* incorporates new classification and measurement requirements for financial assets, the introduction of an expected credit loss impairment model which will replace the incurred loss model of IAS 39 and new hedge accounting requirements. The Group satisfies the criteria set out in IFRS 4 *Insurance Contracts* for the temporary exemption from IFRS 9. At 31 December 2015 (the date specified by IFRS 4), the carrying value of the Group's liabilities connected with insurance comprised over 90% of the total liabilities. These include significant insurance liabilities; the subordinated debt ($0.4 billion) as this debt counts towards the Group's regulatory and rating agency capital requirements; and creditors arising from insurance operations ($0.3 billion). The activities of the Group remain predominately connected with insurance. Based on a high-level impact assessment using currently available information, the Group expects no significant impact on its balance sheet and equity, except for the effect of applying the new impairment requirements. The Group expects a recognition of an earlier and higher loss allowance resulting in a negative impact on equity and will perform a detailed assessment in the future to determine the extent. IFRS 9 has been endorsed by the EU.
- IFRS 16 *Leases* replaces IAS 17 *Leases* and addresses the definition of a lease, recognition and measurement of leases. The adoption of this standard will affect primarily the accounting for the Group's operating leases. As of the reporting date, the estimated discounted non-cancellable operating lease commitments of $79 million would be recognised as an additional asset and liability on the balance sheet. This indicates the impact of the adoption of IFRS 16 on the consolidated financial statements. IFRS 16 is effective from 1 January 2019 and has been endorsed by the EU.
- IFRS 17 will replace IFRS 4 and includes a number of significant changes to the measurement, presentation and disclosure of insurance contracts. It prescribes a general measurement model based on the discounted current estimates of future cash flows, including an explicit risk adjustment and a contractual service margin which represents the unearned profit of the contracts. Application of a simplified premium allocation approach, which is similar to the current unearned premium approach, is permitted if it provides a measurement that is not materially different from the general model or if the coverage period is one year or less. IFRS 17 requires any expected losses arising from loss-making contracts to be accounted for in the income statement when the entity determines that losses are expected. The Group is evaluating the impact of adopting IFRS 17 on the financial statements and the Group's implementation programme is progressing in line with expectations. IFRS 17 is expected to be effective on 1 January 2022 and has not been endorsed by the EU.
- Amendments to IAS 19 *Plan Amendment, Curtailment or Settlement* address the accounting for the current service cost and net interest when a plan amendment, curtailment or settlement occurs during a reporting period. The adoption of these amendments has no impact on the Group's consolidated financial statements These amendments are effective on 1 January 2019 and have not been endorsed by the EU.

2.2 Basis of consolidation

(a) Subsidiaries

Subsidiaries are those entities controlled by the Group. Control exists when the Group has power over an entity, exposure or rights to variable returns from its involvement with the investee and ability to use its power to affect those returns. The consolidated financial statements include the assets, liabilities and results of the Group up to 31 December each year. The financial statements of subsidiaries are included in the consolidated financial statements only from the date that control commences until the date that control ceases.

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred also includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired, liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree on an acquisition-by-acquisition basis, either at fair value or at the non-controlling interest's proportionate share of the recognised amounts of acquiree's identifiable net assets. Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions – that is, as transactions with the owners in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

(b) Associates

Associates are those entities in which the Group has significant influence but not control over the financial and operating policies. Significant influence is generally identified with a shareholding of between 20% and 50% of an entity's voting rights. The consolidated financial statements include the Group's share of the total recognised gains and losses of associates on an equity-accounted basis from the date that significant influence commences until the date that significant influence ceases. The Group's share of its associates' post-acquisition profits or losses after tax is recognised in the income statement for each period, and its share of the movement in the associates' net assets is reflected in the investments' carrying values in the balance sheet. When the Group's share of losses equals or exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

2 Basis of preparation

2.2 Basis of consolidation continued

(c) Transactions eliminated on consolidation

Intragroup balances, transactions and any unrealised gains arising from intragroup transactions are eliminated in preparing the consolidated financial statements. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Foreign currency gains and losses on intragroup monetary assets and liabilities may not fully eliminate on consolidation when the intragroup monetary item concerned is transacted between two Group entities that have different functional currencies. Unrealised gains arising from transactions with associates are eliminated to the extent of the Group's interest in the entity. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

2.3 Foreign currency translation

(a) Functional currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). Entities operating in France, Germany, The Netherlands, Spain, Portugal, Ireland and Belgium have functional currency of Euros; those subsidiary entities operating from the USA, Bermuda, Guernsey and Syndicates have functional currency of US Dollars. Functional currencies of entities operating in Asia include US Dollars, Singapore Dollars and Thai Baht. All other entities have functional currency of Sterling.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the retranslation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as IAS 39 effective net investment hedges or when the underlying balance is deemed to form part of the Group's net investment in a subsidiary operation and is unlikely to be settled in the foreseeable future. Non-monetary items carried at historical cost are translated in the balance sheet at the exchange rate prevailing on the original transaction date. Non-monetary items measured at fair value are translated using the exchange rate ruling when the fair value was determined.

(c) Group companies

The results and financial position of all the Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the date of the transactions); and
- all resulting exchange differences are recognised as a separate component of equity.

When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain, or loss, on sale.

2.4 Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and any impairment loss. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance items are charged to the income statement during the financial period in which they are incurred.

Land is not depreciated as it is deemed to have an indefinite useful economic life. The cost of leasehold improvements is amortised over the unexpired term of the underlying lease or the estimated useful life of the asset, whichever is shorter. Depreciation on other assets is calculated using the straight-line method to allocate their cost, less their residual values, over their estimated useful lives.

The rates applied are as follows:

- buildings 20–50 years
- vehicles 3 years
- leasehold improvements including fixtures and fittings 10–15 years
- furniture, fittings and equipment 3–15 years

The assets' residual values and useful lives are reviewed at each balance sheet date and adjusted if appropriate.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

2.5 Intangible assets

(a) Goodwill

Goodwill represents amounts arising on acquisition of subsidiaries and associates. In respect of acquisitions that have occurred since 1 January 2004, goodwill represents the excess of the fair value of consideration of an acquisition over the fair value of the Group's share of the net identifiable assets and contingent liabilities assumed of the acquired subsidiary or associate at the acquisition date.

In respect of acquisitions prior to 1 January 2004, goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous generally accepted accounting principles.

Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates.

Goodwill is not amortised but is tested at least annually for impairment and carried at cost less accumulated impairment losses.

Goodwill is allocated to the Group's cash-generating units identified according to the smallest identifiable unit to which cash flows are generated.

The impairment review process examines whether or not the carrying value of the goodwill attributable to individual cash-generating units exceeds its recoverable amount. Any excess of goodwill over the recoverable amount arising from the review process indicates impairment. Any impairment charges are presented as part of operational expenses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

(b) Other intangible assets

Intangible assets acquired separately from a business are carried initially at cost. An intangible asset acquired as part of a business combination is recognised outside of goodwill if the asset is separable or arises from contractual

2 Basis of preparation

2.5 Intangible assets

(b) Other intangible assets continued

or other legal rights and its fair value can be measured reliably. Customer relationships, syndicate capacity and software acquired are capitalised at cost, being the fair value of the consideration paid. Software is capitalised on the basis of the costs incurred to acquire and bring it into use. Intangible assets with indefinite lives such as syndicate capacity are subsequently valued at cost and are subject to annual impairment assessment.

Intangible assets with finite useful lives are consequently carried at cost, less accumulated amortisation and impairment. The useful life of the asset is reviewed annually. Any changes in estimated useful lives are accounted for prospectively with the effect of the change being recognised in the current and future periods, if relevant.

Amortisation is calculated using the straight-line method to allocate the cost over the estimated useful lives of the intangible assets.

Subsequent expenditure on other intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Those intangible assets with finite lives are assessed for indicators of impairment at each reporting date. Where there is an indication of impairment then a full impairment test is performed. An impairment loss recognised for an intangible asset in prior years should be reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised.

2.6 Fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique.

This presumes that the transaction takes place in the principal (or most advantageous) market under current market conditions. Fair value is a market-based measure and in the absence of observable market prices in an active market, it is measured using the assumptions that market participants would use when pricing the asset or liability.

The fair value of a non-financial asset is determined based on its highest and best use from a market participant's perspective. When using this approach, the Group takes into account the asset's use that is physically possible, legally permissible and financially feasible. The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received. If an asset or a liability measured at fair value has a bid price and an ask price, the price within the bid-ask spread that is most representative of fair value in the circumstances is used to measure fair value. An analysis of fair values of financial instruments and further details as to how they are measured are provided in note 20.

2.7 Financial assets and liabilities including loans and receivables

The Group classifies its financial assets as a) financial assets at fair value through profit or loss, and b) loans and receivables. Management determines the classification of its financial assets based on the purpose for which the financial assets are held at initial recognition. The decision by the Group to designate debt and fixed income securities, equities and shares in unit trusts and deposits with credit institutions, at fair value through profit or loss reflects the fact that the investment portfolios are managed, and their performance evaluated, on a fair value basis.

Purchases and sales of investments are accounted for at the trade date. Financial assets and liabilities are initially recognised at fair value. Subsequent to initial recognition financial assets and liabilities are measured as described below. Financial assets are derecognised when the right to receive cash flows from them expires or where they have been transferred and the Group has also transferred substantially all risks and rewards of ownership.

(a) Financial assets at fair value through profit or loss

A financial asset is classified into this category at inception if it is managed and evaluated on a fair value basis in accordance with a documented strategy, if acquired principally for the purpose of selling in the short term, or if it forms part of a portfolio of financial assets in which there is evidence of short-term profit taking.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Receivables arising from insurance contracts are included in this category and are reviewed for impairment as part of the impairment review of loans and receivables. Loans and receivables are carried at amortised cost less any provision for impairment in value.

(c) Long-term debt

All borrowings are initially recognised at fair value. Subsequent to initial recognition, borrowings are measured at amortised cost. Any difference between the value recognised at initial recognition and the ultimate redemption amount is recognised in the income statement over the period to redemption using the effective interest method.

2.8 Cash and cash equivalents

The Group has classified cash deposits and short-term highly-liquid investments as cash and cash equivalents. These assets are readily convertible into known amounts of cash and are subject to inconsequential changes in value. Cash equivalents are financial investments with less than three months to maturity at the date of acquisition.

2.9 Impairment of assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually or whenever there is an indication of impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

(a) Non-financial assets

Objective factors that are considered when determining whether a non-financial asset (such as goodwill, an intangible asset or item of property, plant and equipment) or group of non-financial assets may be impaired include, but are not limited to, the following:

- adverse economic, regulatory or environmental conditions that may restrict future cash flows and asset usage and/or recoverability;
- the likelihood of accelerated obsolescence arising from the development of new technologies and products; and
- the disintegration of the active market(s) to which the asset is related.

2 Basis of preparation
2.9 Impairment of assets continued
(b) Financial assets
Objective factors that are considered when determining whether a financial asset or group of financial assets may be impaired include, but are not limited to, the following:
- negative rating agency announcements in respect of investment issuers, reinsurers and debtors;
- significant reported financial difficulties of investment issuers, reinsurers and debtors;
- actual breaches of credit terms such as persistent late payments or actual default;
- the disintegration of the active market(s) in which a particular asset is traded or deployed;
- adverse economic or regulatory conditions that may restrict future cash flows and asset recoverability; and
- the withdrawal of any guarantee from statutory funds or sovereign agencies implicitly supporting the asset.

(c) Impairment loss
An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). For financial assets, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the value of the estimated future cash flows discounted at the financial asset's original effective interest rate. Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior periods. A reversal of an impairment loss is recognised as income immediately. Impairment losses recognised in respect of goodwill are not subsequently reversed.

2.10 Derivative financial instruments
Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently valued at fair value at each balance sheet date. Fair values are obtained from quoted market values and, if these are not available, valuation techniques including option pricing models as appropriate. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. For derivatives not formally designated as a hedging instrument, fair value changes are recognised immediately in the income statement. Changes in the value of derivatives and other financial instruments formally designated as hedges of net investments in foreign operations are recognised in the currency translation reserve to the extent they are effective; gains or losses relating to the ineffective portion of the hedging instruments are recognised immediately in the consolidated income statement.

The Group had no derivative instruments designated for hedge accounting during the current and prior financial year (see note 2.16).

2.11 Own shares
Where any Group company purchases the Parent Company's equity share capital (own shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's owners on consolidation. Where such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity attributable to the Company's owners, net of any directly attributable incremental transaction costs and the related tax effects.

2.12 Revenue
Revenue comprises insurance and reinsurance premiums earned on the rendering of insurance protection, net of reinsurance, together with profit commission, investment returns, agency fees and other income. The Group's share of the results of associates is reported separately. The accounting policies for insurance premiums are set out in note 2.13.

Other revenue is recognised when, or as, the control of the goods or services are transferred to a customer, i.e. performance obligations are fulfilled at an amount that reflects the consideration to which the Group expects to be entitled in exchange for those goods or services. See note 9 for further details.

2.13 Insurance contracts
(a) Classification
Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause an insurer to make significant additional payments in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. The Group issues short-term casualty and property insurance contracts that transfer significant insurance risk.

(b) Recognition and measurement
Gross premiums written comprise premiums on business incepting in the financial year together with adjustments to estimates of premiums written in prior accounting periods. Estimates are included for pipeline premiums and an allowance is also made for cancellations. Premiums are stated before the deduction of brokerage and commission but net of taxes and duties levied. Premiums are recognised as revenue (premiums earned) proportionally over the period of coverage. The portion of premium received on in-force contracts that relate to unexpired risks at the balance sheet date is reported as the unearned premium liability.

Claims and associated expenses are charged to profit or loss as incurred, based on the estimated liability for compensation owed to contract holders or third parties damaged by the contract holders. They include direct and indirect claims settlement costs and arise from events that have occurred up to the balance sheet date even if they have not yet been reported to the Group.

The Group does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are determined based on the best estimate of the cost of future claim payments plus an allowance for risk and uncertainty. Any estimate represents a determination within a range of possible outcomes using, as inputs, the assessments for individual cases reported to the Group, statistical analysis for the claims incurred but not reported, an estimate of the expected ultimate cost of more complex claims that may be affected by external factors, for example, court decisions and an allowance for quantitative uncertainties not otherwise approved.

2 Basis of preparation

2.13 Insurance contracts continued

(c) Deferred acquisition costs (DAC)
Commissions and other direct and indirect costs that vary with and are related to securing new contracts and renewing existing contracts are capitalised as deferred acquisition costs. All other costs are recognised as expenses when incurred. DAC are amortised over the terms of the insurance contracts as the related premium is earned.

(d) Liability adequacy tests
At each balance sheet date, liability adequacy tests are performed by each business unit to ensure the adequacy of the contract liabilities net of related DAC. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from assets backing such liabilities, are used. Any deficiency is charged to profit or loss initially by writing-off DAC and by subsequently establishing a provision for losses arising from liability adequacy tests ('the unexpired risk provision'). Any DAC written-off as a result of this test is not subsequently reinstated.

(e) Outwards reinsurance contracts held
Contracts entered into by the Group with reinsurers, under which the Group is compensated for losses on one or more insurance or reinsurance contracts and that meet the classification requirements for insurance contracts, are classified as insurance contracts held. Contracts that do not meet these classification requirements are classified as financial assets.

The benefits to which the Group is entitled under outwards reinsurance contracts are recognised as reinsurance assets. These assets consist of short-term balances due from reinsurers (classified within loans and receivables) as well as longer-term receivables (classified as reinsurance assets) that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract.

Reinsurance liabilities primarily comprise premiums payable for outwards reinsurance contracts. The Group assesses its reinsurance assets on a regular basis and, if there is objective evidence, after initial recognition, of an impairment in value, the Group reduces the carrying amount of the reinsurance asset to its recoverable amount and recognises the impairment loss in the income statement.

(f) Retroactive reinsurance transactions
Reinsurance transactions that transfer risk but are retroactive are included in reinsurance assets. The excess of estimated liabilities for claims and claim expenses over the consideration paid is established as a deferred credit at inception. The deferred amounts are subsequently amortised using the recovery method over the settlement period of the reserves and reflected through the claims and claim adjustment expenses line. In transactions where the consideration paid exceeds the estimated liabilities for claims and claim adjustment expenses a loss is recognised immediately.

(g) Reinsurance commission income
Reinsurance commission income represents commission earned from ceding companies which is earned over the terms of the underlying reinsurance contracts and presented separately in the consolidated income statement.

(h) Receivables and payables related to insurance contracts
Receivables and payables are recognised when due. These include amounts due to, and from, agents, brokers and insurance contract holders. If there is objective evidence that the insurance receivable is impaired, the Group reduces the carrying amount of the insurance receivable accordingly and recognises the impairment loss in the income statement.

(i) Salvage and subrogation reimbursements
Some insurance contracts permit the Group to sell property acquired in settling a claim (i.e. salvage). The Group may also have the right to pursue third parties for payment of some or all costs (i.e. subrogation). Estimates of salvage recoveries are included as an allowance in the measurement of the insurance liability for claims and salvage property is recognised in other assets when the liability is settled. The allowance is the amount that can reasonably be recovered from the disposal of the property. Subrogation reimbursements are also considered as an allowance in the measurement of the insurance liability for claims and are recognised in other assets when the liability is settled. The allowance is the assessment of the amount that can be recovered from the action against the liable third party.

2.14 Deferred tax

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not recognised. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

2.15 Employee benefits

(a) Pension obligations
The Group operated both defined contribution and defined benefit pension schemes during the year under review. The defined benefit scheme closed to future accrual with effect from 31 December 2006 and active members were offered membership of the defined contribution scheme from 1 January 2007. A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity and has no further obligation beyond the agreed contribution rate. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation.

For defined contribution plans, the Group pays contributions to publicly or privately administered pension insurance plans on a contractual basis.

2 Basis of preparation

2.15 Employee benefits

(a) Pension obligations continued

The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

The amount recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date, less the fair value of plan assets. Plan assets include insurance contracts. The calculation of the defined benefit obligation is performed annually by a qualified actuary using the projected unit method. As the plan is closed to all future benefit accrual, each participant's benefits under the plan are based on their service to the date of closure or earlier leaving, their final pensionable earnings at the measurement date and the service cost is the expected administration cost during the year. Past service costs are recognised immediately in income.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in other comprehensive income. The Group determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognised in the income statement through operating expenses.

To the extent that a surplus emerges on the defined benefit obligation, it is only recognisable as an asset when it is probable that future economic benefits will be recovered by the Group in the form of refunds.

(b) Other long-term employee benefits

The Group provides sabbatical leave to employees on completion of a minimum service period of ten years. The present value of the expected costs of these benefits is accrued over the period of employment. In determining this liability, consideration is given to future increases in salary levels, experience with employee departures and periods of service.

(c) Share-based compensation

The Group operates a number of equity settled share-based employee compensation plans. These include the share option schemes, and the Group's Performance Share Plans, outlined in the Directors' remuneration report together with the Group's Save as You Earn (SAYE) schemes. The fair value of the employee services received, measured at grant date, in exchange for the grant of the awards is recognised as an expense, with the corresponding credit being recorded in retained earnings within equity. The total amount to be expensed over the vesting period is determined by reference to the fair value of the awards granted, excluding the impact of any non-market vesting conditions (for example, profitability or net asset growth targets). Non-market vesting conditions are included in assumptions about the number of awards that are expected to become exercisable. At each balance sheet date, the Group revises its estimates of the number of awards that are expected to vest.

The Group recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity, over the remaining vesting period.

When the terms and conditions of an equity settled share-based employee compensation plan are modified, and the expense to be recognised increases as a result of the modification, then the increase is recognised evenly over the remaining vesting period. When a modification reduces the expense to be recognised, there is no adjustment recognised and the pre-modification expense continues to be applied. The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium when the options are exercised.

(d) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

(e) Profit sharing and bonus plans

The Group recognises a liability and an expense for bonuses and profit sharing, based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The Group recognises a provision where a contractual obligation to employees exists or where there is a past practice that has created a constructive obligation.

(f) Accumulating compensation benefits

The Group recognises a liability and an expense for accumulating compensation benefits (for example, holiday entitlement), based on the additional amount that the Group expects to pay as a result of the unused entitlement accumulated at the balance sheet date.

2.16 Net investment hedge accounting

In order to qualify for hedge accounting, the Group is required to document in advance the relationship between the item being hedged and the hedging instrument. The Group is also required to document and demonstrate an assessment of the relationship between the hedged item and the hedging instrument, which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at each period end to ensure that the hedge remains highly effective. The Group hedged elements of its net investment in certain foreign entities through foreign currency borrowings that qualified for hedge accounting from 3 January 2007 until their replacement on 6 May 2008; accordingly gains or losses on retranslation are recognised in equity to the extent that the hedge relationship was effective during this period. Accumulated gains or losses will be recycled to the income statement only when the foreign operation is disposed of. The ineffective portion of any hedge is recognised immediately in the income statement.

2.17 Finance costs

Finance costs consist of interest charges accruing on the Group's borrowings and bank overdrafts together with commission fees charged in respect of Letters of Credit. Arrangement fees in respect of financing arrangements are charged over the life of the related facilities.

2 Basis of preparation continued

2.18 Provisions

Provisions are recognised where there is a present obligation (legal or constructive) as a result of a past event that can be measured reliably and it is probable that an outflow of economic benefits will be required to settle that obligation.

2.19 Leases

(a) Hiscox as lessee

Leases in which significantly all of the risks and rewards of ownership are transferred to the Group are classified as finance leases. At the commencement of the lease term, finance leases are recognised as assets and liabilities at the lower of the fair value of the asset and the present value of the minimum lease payments. The minimum lease payments are apportioned between finance charges and repayments of the outstanding liability, finance charges being charged to each period of the lease term so as to produce a constant rate of interest on the outstanding balance of the liability. All other leases are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

(b) Hiscox as lessor

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant contractual agreement.

2.20 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved.

2.21 Use of significant judgements, estimates and assumptions

The preparation of financial statements requires the Group to select accounting policies and make judgements, estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses in the consolidated financial statements.

The Audit Committee reviews the reasonableness of critical judgements, estimates and assumptions applied and the appropriateness of significant accounting policies. The significant issues considered by the Committee in the year are included within the Audit Committee report on pages 65 to 66.

Critical accounting judgements

The following accounting policies are those considered to have a significant impact on the amounts recognised in the consolidated financial statements, with those judgements involving estimation summarised thereafter.

- Consolidation: assessment of whether the Group controls an underlying entity, for example, the treatment of insurance-linked securities funds including consideration of its decision-making authority and its rights to the variable returns from the entity;
- Insurance contract: assessment of the significance of insurance risk transferred to the Group in determining whether a contract should be accounted for as an insurance contract or as a financial instrument;
- Financial investments: classification and measurement of investments including the application of the fair value option.

Significant accounting estimates

All estimates are based on management's knowledge of current facts and circumstances, assumptions based on that knowledge and their predictions of future events. Actual results may differ from those estimates, possibly significantly.

Estimates are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The following describes items considered particularly susceptible to changes in estimates and assumptions.

The most critical estimate included within the Group's balance sheet is the estimate for losses incurred but not reported. The total gross estimate as at 31 December 2018 is $3,035 million (2017: $2,724 million) and is included within total insurance liabilities on the balance sheet.

Estimates of losses incurred but not reported are continually evaluated, based on entity-specific historical experience and contemporaneous developments observed in the wider industry when relevant, and are also updated for expectations of prospective future developments. Although the possibility exists for material changes in estimates to have a critical impact on the Group's reported performance and financial position, it is anticipated that the scale and diversity of the Group's portfolio of insurance business considerably lessens the likelihood of this occurring. The overall reserving risk is discussed in more detail in note 3.1 and the procedures used in estimating the cost of settling insured losses at the balance sheet date including losses incurred but not reported are detailed in note 23.

The Group carries its financial investments at fair value through profit or loss, with fair values determined using published price quotations in the most active financial markets in which the assets trade, where available. Where quoted market prices are not available, valuation techniques are used to value financial instruments. These include broker quotes and models utilising broker quotes and models using both observable and unobservable market inputs. The valuation techniques involve judgement with regard to the valuation models used and the inputs to these models can lead to a range of plausible valuation for financial investments. Note 3.2(a) discusses the reliability of the Group's fair values.

The employee retirement benefit scheme obligations are calculated and valued with reference to a number of actuarial assumptions including mortality, inflation rates and discount rate, many of which have been subject to specific recent volatility. This complex set of economic variables can have a significant impact on the financial statements, as shown in note 27.

A deferred tax asset can be recognised only to the extent that it is recoverable. The recoverability of deferred tax assets in respect of carry forward losses requires consideration of the future levels of taxable profit in the Group. In preparing the Group's financial statements, management estimates taxation assets and liabilities after taking appropriate professional advice, as shown in note 25. Significant estimates and assumptions used in the valuation of deferred tax relate to the forecast taxable profits, taking into account the Group's financial and strategic plans. The determination and finalisation of agreed taxation assets and liabilities may not occur until several years after the reporting date and consequently the final amounts payable or receivable may differ from those presented in these financial statements.

2 Basis of preparation continued

2.22 Reporting of additional performance measures

The Directors consider that the profit excluding foreign exchange gains/(losses), the claims ratio, expense ratio and combined ratio measures reported in respect of operating segments and the Group overall in note 4 provide useful information regarding the underlying performance of the Group's businesses. These measures are widely recognised by the insurance industry and are consistent with internal performance measures reviewed by senior management including the chief operating decision-maker. However, these four measures are not defined within the IFRS framework and body of standards and interpretations and therefore may not be directly comparable with similarly titled additional performance measures reported by other companies. Net asset value per share and return on equity measures, disclosed in notes 5 and 6, are likewise considered to be additional performance measures.

3 Management of risk

The Group's overall appetite for accepting and managing varying classes of risk is defined by the Group's Board of Directors. The Board has developed a governance framework and has set Group-wide risk management policies and procedures which include risk identification, risk management and mitigation and risk reporting. The objective of these policies and procedures is to protect the Group's shareholders, policyholders and other stakeholders from negative events that could hinder the Group's delivery of its contractual obligations and its achievement of sustainable profitable economic and social performance.

The Board exercises oversight of the development and operational implementation of its risk management policies and procedures through the Risk Committee and ongoing compliance therewith, through a dedicated internal audit function, which has operational independence, clear terms of reference influenced by the Board's Non Executive Directors and a clear upwards reporting structure back into the Board. The Group, in common with the non-life insurance industry generally, is fundamentally driven by a desire to originate, retain and service insurance contracts to maturity. The Group's cash flows are funded mainly through advance premium collections and the timing of such premium inflows is reasonably predictable. In addition, the majority of material cash outflows are typically triggered by the occurrence of insured events non-correlated to financial markets, and not by the inclination or will of policyholders.

The principal sources of risk relevant to the Group's operations and its financial statements fall into two broad categories: insurance risk and financial risk, which are described in notes 3.1 and 3.2 below. The Group also actively manages its capital risks as detailed in note 3.3 and tax risks as detailed in note 3.4. Additional unaudited information is also provided in the corporate governance, risk management and capital sections of this Report and Accounts.

3.1 Insurance risk

The predominant risk to which the Group is exposed is insurance risk which is assumed through the underwriting process. Insurance risk can be sub-categorised into i) underwriting risk including the risk of catastrophe and systemic insurance losses and the insurance competition and cycle, and ii) reserving risk.

i) Underwriting risk

The Board sets the Group's underwriting strategy and risk appetite seeking to exploit identified opportunities in the light of other relevant anticipated market conditions.

The Board requires all underwriters to operate within an overall Group appetite for individual events. This defines the maximum exposure that the Group is prepared to retain on its own account for any one potential catastrophe event or disaster. The Group's underwriting risk appetite seeks to ensure that it should not lose more than 12.5% of core capital, defined as NAV plus subordinated debt less expected dividend less buffer capital, plus 100% of buffer capital ($135 million) with an allowance for expected investment income, as a result of a 1 in 200 aggregate bad underwriting year.

Specific underwriting objectives such as aggregation limits, reinsurance protection thresholds, geographical disaster event risk exposures and line of business diversification parameters are prepared and reviewed by the Chief Underwriting Officer in order to translate the Board's summarised underwriting strategy into specific measurable actions and targets. These actions and targets are reviewed and approved by the Board in advance of each underwriting year. The Board continually reviews its underwriting strategy throughout each underwriting year in light of the evolving market pricing and loss conditions and as opportunities present themselves. The Group's underwriters and management consider underwriting risk at an individual contract level, and also from a portfolio perspective where the risks assumed in similar classes of policies are aggregated and the exposure evaluated in light of historical portfolio experience and prospective factors. To assist with the process of pricing and managing underwriting risk the Group routinely performs a wide range of activities including the following:

- regularly updating the Group's risk models;
- documenting, monitoring and reporting on the Group's strategy to manage risk;
- developing systems that facilitate the identification of emerging issues promptly;
- utilising sophisticated computer modelling tools to simulate catastrophes and measure the resultant potential losses before and after reinsurance;
- monitoring legal developments and amending the wording of policies when necessary;
- regularly aggregating risk exposures across individual underwriting portfolios and known accumulations of risk;
- examining the aggregated exposures in advance of underwriting further large risks; and
- developing processes that continually factor market intelligence into the pricing process.

The delegation of underwriting authority to specific individuals, both internally and externally, is subject to regular review. All underwriting staff and binding agencies are set strict parameters in relation to the levels and types of business they can underwrite, based on individual levels of experience and competence. These parameters cover areas such as the maximum sums insured per insurance contract, maximum gross premiums written and maximum aggregated exposures per geographical zone and risk class. Regular meetings are held between the Chief Underwriting Officer and a specialist team in order to monitor claim development patterns and discuss individual underwriting issues as they arise.

The Group compiles estimates of losses arising from realistic disaster events using statistical models alongside input from its underwriters. These require significant management judgement.

3 Management of risk

3.1 Insurance risk

i) Underwriting risk continued

Realistic disaster scenarios, shown on page 21, are extreme hypothetical events selected to represent major events occurring in areas with large insured values. They also reflect the areas that represent significant exposures for Hiscox.

The selection of realistic disaster scenario events is adjusted each year and they are not therefore necessarily directly comparable from one year to the next. The events are extreme and unprecedented, and as such these estimates may prove inadequate as a result of incorrect assumptions, model deficiencies, or losses from unmodelled risks. This means that should a realistic disaster actually eventuate, the Group's final ultimate losses could materially differ from those estimates modelled by management. The Group's insurance contracts include provisions to contain losses, such as the ability to impose deductibles and demand reinstatement premiums in certain cases. In addition, in order to manage the Group's exposure to repeated catastrophic events, relevant policies frequently contain payment limits to cap the maximum amount payable from these insured events over the contract period.

The Group also manages underwriting risk by purchasing reinsurance. Reinsurance protection, such as excess of loss cover, is purchased at an entity level and is also considered at an overall Group level to mitigate the effect of catastrophes and unexpected concentrations of risk. However, the scope and type of reinsurance protection purchased may change depending on the extent and competitiveness of cover available in the market.

Below is a summary of the gross and net insurance liabilities for each category of business.

Estimated concentration of gross and net insurance liabilities on balance sheet 31 December 2018		Types of insurance risk in the Group						
		Reinsurance inwards $000	Property – marine and major assets $000	Property – other assets $000	Casualty – professional indemnity $000	Casualty – other risks $000	Other* $000	Total $000
Total	Gross	1,999,630	263,676	1,034,025	2,099,965	806,102	498,077	6,701,475
	Net	483,829	209,327	684,330	1,785,331	660,776	421,307	4,244,900

Estimated concentration of gross and net insurance liabilities on balance sheet 31 December 2017 (restated)†		Types of insurance risk in the Group						
		Reinsurance inwards $000	Property – marine and major assets $000	Property – other assets $000	Casualty – professional indemnity $000	Casualty – other risks $000	Other* $000	Total $000
Total	Gross	1,497,680	317,980	1,151,814	1,876,068	640,918	523,290	6,007,750
	Net	468,314	253,714	733,235	1,744,629	520,556	454,047	4,174,495

*Includes a diverse mix of certain specialty lines such as kidnap and ransom, terrorism and other risks which contain a mix of property and casualty exposures.
†See note 2.1 for further details.

The estimated liquidity profile to settle the gross claims liabilities is given in note 3.2(e).

The specific insurance risks accepted by the Group fall broadly into the following main categories: reinsurance inwards, marine and major asset property, other property risks, professional indemnity casualty and casualty other insurance risks. These specific categories are defined for risk review purposes only, as each contains risks specific to the nature of the cover provided. They are not exclusively aligned to any specific reportable segment in the Group's operational structure or the primary internal reports reviewed by the chief operating decision-maker. The following describes the policies and procedures used to identify and measure the risks associated with each individual category of business.

Reinsurance inwards

The Group's reinsurance inwards acceptances are primarily focused on large commercial property, homeowner and marine and crop exposures held by other insurance companies predominantly in North America and other developed economies. This business is characterised more by large claims arising from individual events or catastrophes than the high-frequency, low-severity attritional losses associated with certain other business written by the Group. Multiple insured losses can periodically arise out of a single natural or man-made occurrence. The main circumstances that result in claims against the reinsurance inwards book are conventional catastrophes, such as earthquakes or storms, and other events including fires and explosions. The occurrence and impact of these events are very difficult to model over the short term which complicates attempts to anticipate loss frequencies on an annual basis. In those years where there is a low incidence of severe catastrophes, loss frequencies on the reinsurance inwards book can be relatively low.

A significant proportion of the reinsurance inwards business provides cover on an excess of loss basis for individual events. The Group agrees to reimburse the cedant once their losses exceed a minimum level. Consequently the frequency and severity of reinsurance inwards claims are related not only to the number of significant insured events that occur but also to their individual magnitude. If numerous catastrophes occurred in any one year, but the cedant's individual loss on each was below the minimum stated, then the Group would have no liability under such contracts. Maximum gross line sizes and aggregate exposures are set for each type of programme.

The Group writes reinsurance risks for periods of mainly one year so that contracts can be assessed for pricing and terms and adjusted to reflect any changes in market conditions.

3 Management of risk

3.1 Insurance risk

i) Underwriting risk continued

Property risks – marine and major assets

The Group directly underwrites a diverse range of property risks. The risk profile of the property covered under marine and major asset policies is different to that typically contained in the other classes of property (such as private households and contents insurance) covered by the Group.

Typical property covered by marine and other major property contracts includes fixed and moveable assets such as ships and other vessels, cargo in transit, energy platforms and installations, pipelines, other subsea assets, satellites, commercial buildings and industrial plants and machinery. These assets are typically exposed to a blend of catastrophic and other large loss events and attritional claims arising from conventional hazards such as collision, flooding, fire and theft. Climatic changes may give rise to more frequent and severe extreme weather events (for example windstorms and river flooding) and it may be expected that their frequency will increase over time.

For this reason the Group accepts major property insurance risks for periods of mainly one year so that each contract can be repriced on renewal to reflect the continually evolving risk profile. The most significant risks covered for periods exceeding one year are certain specialist lines such as marine and offshore construction projects which can typically have building and assembling periods of between three and four years. These form a small proportion of the Group's overall portfolio.

Marine and major property contracts are normally underwritten by reference to the commercial replacement value of the property covered. The cost of repairing or rebuilding assets, of replacement or indemnity for contents and time taken to restart or resume operations to original levels for business interruption losses are the key factors that influence the level of claims under these policies. The Group's exposure to commodity price risk in relation to these types of insurance contracts is very limited, given the controlled extent of business interruption cover offered in the areas prone to losses of asset production.

Other property risks

The Group provides home and contents insurance, together with cover for artwork, antiques, classic cars, jewellery, collectables and other assets. The Group also extends cover to reimburse certain policyholders when named insureds or insured assets are seized for kidnap and a ransom demand is subsequently met. Events which can generate claims on these contracts include burglary, kidnap, seizure of assets, acts of vandalism, fires, flooding and storm damage. Losses on most classes can be predicted with a greater degree of certainty as there is a rich history of actual loss experience data and the locations of the assets covered, and the individual levels of security taken by owners, are relatively static from one year to the next. The losses associated with these contracts tend to be of a higher frequency and lower severity than the marine and other major property assets covered above.

The Group's home and contents insurance contracts are exposed to weather and climatic risks such as floods and windstorms and their consequences. As outlined earlier the frequency and severity of these losses do not lend themselves to accurate prediction over the short term. Contract periods are therefore not normally more than one year at a time to enable risks to be regularly repriced.

Contracts are underwritten by reference to the commercial replacement value of the properties and contents insured. Claims payment limits are always included to cap the amount payable on occurrence of the insured event.

Casualty insurance risks

The casualty underwriting strategy attempts to ensure that the underwritten risks are well diversified in terms of type and amount of potential hazard, industry and geography. However, the Group's exposure is more focused towards marine, professional, general and technological liability risks rather than human bodily injury risks, which are only accepted under limited circumstances. Claims typically arise from incidents such as errors and omissions attributed to the insured, professional negligence and specific losses suffered as a result of electronic or technological failure of software products and websites.

The provision of insurance to cover allegations made against individuals acting in the course of fiduciary or managerial responsibilities, including directors and officers' insurance, is one example of a casualty insurance risk. The Group's casualty insurance contracts mainly experience low severity attritional losses. By nature, some casualty losses may take longer to settle than the other categories of business.

The Group's pricing strategy for casualty insurance policies is typically based upon historical claim frequencies and average claim severities, adjusted for inflation and extrapolated forwards to incorporate projected changes in claims patterns. In determining the price of each policy an allowance is also made for acquisition and administration expenses, reinsurance costs, investment returns and the Group's cost of capital.

ii) Reserving risk

The Group's procedures for estimating the outstanding costs of settling insured losses at the balance sheet date, including claims incurred but not yet reported, are detailed in note 23.

The Group's provision estimates are subject to rigorous review by senior management from all areas of the business. The managed syndicates and USA business receive a review of their estimates from independent actuaries. The final provision is approved by the relevant boards on the recommendation of dedicated reserving committees.

Similar to the underwriting risk detailed above, the Group's reserve risks are well diversified. The short-tailed claims are normally notified and settled within 12 to 24 months of the insured event occurring. Those claims taking the longest time to develop and settle typically relate to casualty risks where legal complexities occasionally develop regarding the insured's alleged omissions or negligence. The length of time required to obtain definitive legal judgements and make eventual settlements exposes the Group to a degree of reserving risk in an inflationary environment.

The majority of the Group's casualty exposures are written on a claims-made basis. However the final quantum of these claims may not be established for a number of years after the event. Consequently a significant proportion of the casualty insurance amounts reserved on the balance sheet may not be expected to settle within 24 months of the balance sheet date.

Certain marine and property insurance contracts, such as those relating to subsea and other energy assets and the related business interruption risks, can also take longer than normal to settle. This is because of the length of time required for detailed subsea surveys to be carried out and damage assessments agreed together with difficulties in predicting when the assets can be brought back into full production.

3 Management of risk
3.1 Insurance risk
ii) Reserving risk continued

For the inwards reinsurance lines, there is often a time lag between the establishment and re-estimate of case reserves and reporting to the Group. The Group works closely with the reinsured to ensure timely reporting and also centrally analyses industry loss data to verify the reported reserves.

3.2 Financial risk
Overview

The Group is exposed to financial risk through its ownership of financial instruments including financial liabilities. These items collectively represent a significant element of the Group's net shareholder funds. The Group invests in financial assets in order to fund obligations arising from its insurance contracts and financial liabilities.

The key financial risk for the Group is that the proceeds from its financial assets and investment result generated thereon are not sufficient to fund the obligations. The most important elements and economic variables that could result in such an outcome relate to the reliability of fair value measures, equity price risk, interest rate risk, credit risk, liquidity risk and currency risk. The Group's policies and procedures for managing exposure to these specific categories of risk are detailed below.

(a) Reliability of fair values

The Group has elected to carry loans and receivables at amortised cost and all financial investments at fair value through profit or loss as they are managed and evaluated on a fair value basis in accordance with a documented strategy. With the exception of unquoted equity investments and the insurance-linked funds shown in note 20, all of the financial investments held by the Group are available to trade in markets and the Group therefore seeks to determine fair value by reference to published prices or as derived by pricing vendors using observable quotations in the most active financial markets in which the assets trade. The fair value of financial assets is measured primarily with reference to their closing bid-market prices at the balance sheet date. The ability to obtain quoted bid-market prices may be reduced in periods of diminished liquidity. In addition, those quoted prices that may be available may represent an unrealistic proportion of market holdings or individual trade sizes that could not be readily available to the Group. In such instances fair values may be determined or partially supplemented using other observable market inputs such as prices provided by market makers such as dealers and brokers, and prices achieved in the most recent regular transaction of identical or closely related instruments occurring before the balance sheet date but updated for relevant perceived changes in market conditions.

At 31 December 2018, the Group holds asset-backed and mortgage-backed fixed income instruments in its investment portfolio, but has minimal direct exposure to sub-prime asset classes. Together with the Group's investment managers, management continues to monitor the potential for any adverse development associated with this investment exposure through the analysis of relevant factors such as credit ratings, collateral, subordination levels and default rates in relation to the securities held. The Group did not experience any material defaults on debt securities during the year.

Valuation of these securities will continue to be impacted by external market factors including default rates, rating agency actions, and liquidity. The Group will make adjustments to the investment portfolio as appropriate as part of its overall portfolio strategy, but its ability to mitigate its risk by selling or hedging its exposures may be limited by the market environment. The Group's future results may be impacted, both positively and negatively, by the valuation adjustments applied to these securities.

Note 20 provides an analysis of the measurement attributes of the Group's financial instruments.

(b) Equity price risk

The Group is exposed to equity price risk through its holdings of equity and unit trust investments. This is limited to a relatively small and controlled proportion of the overall investment portfolio and the equity and unit trust holdings involved are diversified over a number of companies and industries. The fair value of equity assets in the Group's balance sheet at 31 December 2018 was $398 million (2017: $451 million). These may be analysed as follows:

Nature of equity and unit trust holdings	2018 % weighting	2017 % weighting
Directly held equity securities	4	3
Units held in funds – traditional long only	58	67
Units held in funds – long and short and special strategies	38	30
Geographic focus		
Specific UK mandates	36	43
Global mandates	64	57

The allocation of equity risk is not heavily confined to any one market index so as to reduce the Group's exposure to individual sensitivities. We make an allocation to less volatile, absolute return strategies within our risk assets, so as to balance our desire to maximise returns with the need to ensure capital is available to support our underwriting throughout any downturn in financial markets. A 10% downward correction in equity prices at 31 December 2018 would have been expected to reduce Group equity and profit after tax for the year by approximately $36.4 million (2017: $39.3 million) assuming that the only area impacted was equity financial assets. A 10% upward movement is estimated to have an equal but opposite effect.

(c) Interest rate risk

Fixed income investments represent a significant proportion of the Group's assets and the Board continually monitors investment strategy to minimise the risk of a fall in the portfolio's market value which could affect the amount of business that the Group is able to underwrite or its ability to settle claims as they fall due. The fair value of the Group's investment portfolio of debt and fixed income securities is normally inversely correlated to movements in market interest rates. If market interest rates rise, the fair value of the Group's debt and fixed income investments would tend to fall and vice versa if credit spreads remained constant. Debt and fixed income assets are predominantly invested in high-quality corporate, government and asset-backed bonds. The investments typically have relatively short durations and terms to maturity. The portfolio is managed to minimise the impact of interest rate risk on anticipated Group cash flows.

The Group may also, from time to time, enter into interest rate future contracts in order to reduce interest rate risk on specific portfolios. The fair value of debt and fixed income assets in the Group's balance sheet at 31 December 2018 was $4,575 million (2017: $4,631 million).

3 Management of risk
3.2 Financial risk
(c) Interest rate risk continued

These may be analysed below as follows:

Nature of debt and fixed income holdings	2018 % weighting	2017 % weighting
Government issued bonds and instruments	33	34
Agency and government supported debt	10	14
Asset-backed securities	2	3
Mortgage-backed instruments – agency	3	4
Mortgage-backed instruments – non-agency	1	1
Mortgage-backed instruments – commercial	–	1
Corporate bonds	49	40
Lloyd's deposits and bond funds	2	3

One method of assessing interest rate sensitivity is through the examination of duration-convexity factors in the underlying portfolio. Using a duration-convexity-based sensitivity analysis, if market interest rates had risen by 100 basis points at the balance sheet date,the Group equity and profit after tax for the year might have been expected to decrease by approximately $69 million (2017: $68 million) assuming that the only balance sheet area impacted was debt and fixed income financial assets. Duration is the weighted average length of time required for an instrument's cash flow stream to be recovered, where the weightings involved are based on the discounted present values of each cash flow. A closely related concept, modified duration, measures the sensitivity of the instrument's price to a change in its yield to maturity. Convexity measures the sensitivity of modified duration to changes in the yield to maturity. Using these three concepts, scenario modelling derives the above estimated impact on instruments' fair values for a 100 basis point change in the term structure of market interest rates.

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest-bearing. The Group's debt and fixed income assets are further detailed at note 17.

At 31 December 2018, no cash was drawn on the Group's borrowing facility (2017: $nil). At 31 December 2018, the Group had long-term debt of £550 million (2017: £275 million). The £550 million consists of two listed instruments of £275 million each, as explained in note 17: the first being fixed-to-floating rate notes where the floating rate becomes effective from November 2025; the second being fixed rate notes maturing in December 2022. The Group has no other significant borrowings or other assets or liabilities carrying interest rate risk, other than the facilities and Letters of Credit outlined in note 30.

(d) Credit risk

The Group has exposure to credit risk, which is the risk that a counterparty will suffer a deterioration in perceived financial strength or be unable to pay amounts in full when due. The concentrations of credit risk exposures held by insurers may be expected to be greater than those associated with other industries, due to the specific nature of reinsurance markets and the extent of investments held in financial markets. In both markets, the Group interacts with a number of counterparties who are engaged in similar activities with similar customer profiles, and often in the same geographical areas and industry sectors. Consequently, as many of these counterparties are themselves exposed to similar economic characteristics, one single localised or macroeconomic change could severely disrupt the ability of a significant number of counterparties to meet the Group's agreed contractual terms and obligations.

Key areas of exposure to credit risk include:
- reinsurers' share of insurance liabilities;
- amounts due from reinsurers in respect of claims already paid;
- amounts due from insurance contract holders; and
- counterparty risk with respect to cash and cash equivalents, and investments including deposits, derivative transactions and catastrophe bonds.

The Group's maximum exposure to credit risk is represented by the carrying values of financial assets and reinsurance assets included in the consolidated balance sheet at any given point in time. The Group does not use credit derivatives or other products to mitigate maximum credit risk exposures on reinsurance assets, but collateral may be requested to be held against these assets. The Group structures the levels of credit risk accepted by placing limits on its exposure to a single counterparty, or groups of counterparties, and having regard to geographical locations. Such risks are subject to an annual or more frequent review. There is no significant concentration of credit risk with respect to loans and receivables, as the Group has a large number of internationally dispersed debtors with unrelated operations. Reinsurance is used to contain insurance risk. This does not, however, discharge the Group's liability as primary insurer. If a reinsurer fails to pay a claim for any reason, the Group remains liable for the payment to the policyholder. The creditworthiness of reinsurers is therefore continually reviewed throughout the year.

The Group Credit Committee assesses the creditworthiness of all reinsurers by reviewing credit grades provided by rating agencies and other publicly available financial information detailing their financial strength and performance as well as detailed analysis from the Group's internal credit analysis team. The financial analysis of reinsurers produces an assessment categorised by S&P rating (or equivalent when not available from S&P).

Despite the rigorous nature of this assessment exercise, and the resultant restricted range of reinsurance counterparties with acceptable strength and credit credentials that emerges therefrom, some degree of credit risk concentration remains inevitable.

The Committee considers the reputation of its reinsurance partners and also receives details of recent payment history and the status of any ongoing negotiations between Group companies and these third parties.

This information is used to update the reinsurance purchasing strategy. Individual operating units maintain records of the payment history for significant brokers and contract holders with whom they conduct regular business. The exposure to individual counterparties is also managed by other mechanisms, such as the right of offset, where counterparties are both debtors and creditors of the Group, and obtaining collateral from unrated counterparties. Management information reports detail provisions for impairment on loans and receivables and subsequent write-off. Exposures to individual intermediaries and groups of intermediaries are collected within the ongoing monitoring of the controls associated with regulatory solvency.

3 Management of risk
3.2 Financial risk
(d) Credit risk continued

The Group also mitigates counterparty credit risk by concentrating debt and fixed income investments in high-quality instruments, including a particular emphasis on government bonds issued mainly by North American countries and the European Union. The Group has no direct exposure to sovereign debt in Spain, Italy, Ireland, Greece or Portugal.

An analysis of the Group's major exposures to counterparty credit risk excluding loans and receivables, and equities and units in unit trusts, based on S&P or equivalent rating, is presented below:

As at 31 December 2018	Note	AAA $000	AA $000	A $000	Other/ non-rated $000	Total $000
Debt and fixed income securities	17	762,117	1,951,770	1,044,053	816,689	4,574,629
Deposits with credit institutions	17	–	–	–	364	364
Reinsurance assets	16	846,409	351,447	1,236,746	21,973	2,456,575
Cash and cash equivalents	21	174,700	115,160	820,708	178,283	1,288,851
Total		1,783,226	2,418,377	3,101,507	1,017,309	8,320,419

As at 31 December 2017 (restated)*	Note	AAA $000	AA $000	A $000	Other/ non-rated $000	Total $000
Debt and fixed income securities	17	810,765	2,207,520	932,926	679,617	4,630,828
Deposits with credit institutions	17	–	2,554	3,503	1,125	7,182
Reinsurance assets	16	492,846	289,757	1,045,912	4,740	1,833,255
Cash and cash equivalents	21	158,685	45,495	637,940	25,647	867,767
Total		1,462,296	2,545,326	2,620,281	711,129	7,339,032

*See note 2.1 for further details.

Within the fixed income portfolios, which include debt securities, deposits with credit institutions and cash equivalent assets, there are exposures to a range of government borrowers, on either a direct or guaranteed basis and banking institutions. The Group, together with its investment managers, closely manages its geographical exposures across government issued and supported debt.

The largest aggregated counterparty exposure related to debt and fixed income securities holdings at 31 December 2018 of $1,214 million is to the US Treasury (2017: $1,254 million).

The Group is exposed to concentrations of risk with individual reinsurers due to the nature of the reinsurance market and the restricted range of reinsurers that have acceptable credit ratings. The largest counterparty exposure included in reinsurance assets at 31 December 2018 is to Kiskadee. The fully collateralised recoverable from Kiskadee represents 17% (2017: 12%) of this category of assets.

Other/non-rated assets include $946 million rated as BBB (2017: $624 million). For the current period and prior period, the Group did not experience any material defaults on debt securities. The Group's AAA rated reinsurance assets include fully collateralised positions at 31 December 2018 and 2017.

(e) Liquidity risk

The Group is exposed to daily calls on its available cash resources, mainly from claims arising from insurance and reinsurance contracts. Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The Board sets limits on the minimum level of cash and maturing funds available to meet such calls and on the minimum level of borrowing facilities that should be in place to cover unexpected levels of claims and other cash demands.

A significant proportion of the Group's investments is in highly liquid assets which could be converted to cash in a prompt fashion and at minimal expense. The deposits with credit institutions largely comprise short-dated certificates for which an active market exists and which the Group can easily access. The Group's exposure to equities is concentrated on shares and funds that are traded on internationally recognised stock exchanges.

The main focus of the investment portfolio is on high-quality, short-duration debt and fixed income securities and cash. There are no significant holdings of investments with specific repricing dates. Notwithstanding the regular interest receipts and also the Group's ability to liquidate these securities and the majority of its other financial instrument assets for cash in a prompt and reasonable manner, the contractual maturity profile of the fair value of these securities at 31 December is as follows on page 122.

3 Management of risk
3.2 Financial risk
(e) Liquidity risk continued

Fair values at balance sheet date analysed by contractual maturity	Less than one year $000	Between one and two years $000	Between two and five years $000	Over five years $000	**2018 Total $000**	2017 Total (restated)* $000
Debt and fixed income securities	1,298,230	1,538,745	1,419,801	317,853	**4,574,629**	4,630,828
Deposits with credit institutions	364	–	–	–	**364**	7,182
Cash and cash equivalents	1,288,851	–	–	–	**1,288,851**	867,767
Total	2,587,445	1,538,745	1,419,801	317,853	**5,863,844**	5,505,777

*See note 2.1 for further details.

The Group's equities and shares in unit trusts and other non-dated instruments have no contractual maturity terms but could also be liquidated in an orderly manner for cash in a prompt and reasonable time frame within one year of the balance sheet date.

The available headroom of working capital is monitored through the use of a detailed Group cash flow forecast which is reviewed by management quarterly or more frequently as required.

Average contractual maturity analysed by denominational currency of investments as at 31 December	**2018 Years**	2017 Years
US Dollar	**2.66**	3.63
Pound Sterling	**2.78**	3.67
Euro	**1.86**	2.39
Canadian Dollar	**1.71**	1.92

The following is an analysis by liability type of the estimated timing of net cash flows based on the gross claims liabilities held. The Group does not discount claims liabilities. The estimated phasing of settlement is based on current estimates and historical trends and the actual timing of future settlement cash flows may differ materially from the disclosure below.

Liquidity requirements to settle estimated profile of gross claim liabilities on balance sheet	Within one year $000	Between one and two years $000	Between two and five years $000	Over five years $000	**2018 Total $000**
Reinsurance inwards	821,066	512,560	355,978	74,076	**1,763,680**
Property – marine and major assets	109,658	56,105	42,504	9,497	**217,764**
Property – other assets	340,363	173,904	70,146	10,283	**594,696**
Casualty – professional indemnity	463,014	455,333	417,136	148,893	**1,484,376**
Casualty – other risks	191,491	126,371	225,080	102,929	**645,871**
Other*	209,670	49,942	24,843	1,361	**285,816**
Total	**2,135,262**	**1,374,215**	**1,135,687**	**347,039**	**4,992,203**

Liquidity requirements to settle estimated profile of gross claim liabilities on balance sheet	Within one year $000	Between one and two years $000	Between two and five years $000	Over five years $000	2017 Total (restated)† $000
Reinsurance inwards	586,487	365,078	277,262	63,287	1,292,114
Property – marine and major assets	114,883	70,431	58,551	15,370	259,235
Property – other assets	357,323	208,053	95,194	11,139	671,709
Casualty – professional indemnity	404,894	388,719	360,392	137,259	1,291,264
Casualty – other risks	156,269	117,437	189,927	73,536	537,169
Other*	201,809	51,735	36,900	8,631	299,075
Total	1,821,665	1,201,453	1,018,226	309,222	4,350,566

*Includes a diverse mix of certain specialty lines such as kidnap and ransom, terrorism and other risks which contain a mix of property and casualty exposures.
†See note 2.1 for further details.

Details of the payment profile of the Group's borrowings, derivative instruments and other liabilities are given in notes 17, 19 and 24.

(f) Currency risk
Currency risk is the risk of loss resulting from fluctuations in exchange rates. The Group operates internationally and therefore is exposed to the financial impact of fluctuations in the exchange rates of various currencies.

The Group's exposures to foreign exchange risk arise mainly with respect to the US Dollar, Pound Sterling and the Euro. These exposures may be classified in two main categories:
- operational foreign exchange exposure arises from the conversion of foreign currency transactions resulting from the activities of entering into insurance, investment and operational contracts in a currency that is different to each respective entity's functional currency; and
- structural foreign exchange exposure arises from the translation of the Group's net investment in foreign operations to the US Dollar, the Group's reporting currency.

3 Management of risk
3.2 Financial risk
(f) Currency risk continued
Operational currency risk

Operational foreign exchange risk is principally managed within the Group's individual entities by broadly matching assets and liabilities by currency and liquidity. Due attention is paid to local regulatory solvency and risk-based capital requirements. All foreign currency derivative transactions with external parties are managed centrally.

The Group does not hedge operational foreign exchange risk arising from the accounting mismatch due to the translation of monetary and non-monetary items. Non-monetary items including unearned premiums, deferred acquisition costs and reinsurers' share of unearned premiums, are recorded at historical transaction rates and are not remeasured at the reporting date. Monetary items including claims reserves, reinsurers' share of claims reserves, and investments are remeasured at each reporting date at the closing rates.

Structural currency risk

Following the change in the Group's presentation currency detailed in note 2.1, the Group's exposure to structural currency risks relates to the Pound Sterling and Euro net investments in businesses operating in the UK and Europe. The Group's risk appetite permits the acceptance of structural foreign exchange movements within defined aggregate limits and exchange rate parameters which are monitored centrally. However, the Group does not ordinarily seek to use derivatives to mitigate the structural risk because:
- the currency translation gains and losses are accounted for in the currency translation reserve (a component of equity) and does not affect income statement unless the related foreign operation is disposed of;
- the currency translation gains and losses have no cash flow.

In periods of significant volatility that are expected to persist for an extended period of time, the Group may elect to utilise derivatives to mitigate or reduce the risk in order to preserve capital.

The currency profile of the Group's assets and liabilities is as follows:

As at 31 December 2018	US Dollar $000	Sterling $000	Euro $000	Other $000	Total $000
Goodwill and intangible assets	37,149	164,876	–	2,575	204,600
Property, plant and equipment	5,553	50,107	4,760	1,038	61,458
Investments in associates	–	9,409	513	–	9,922
Deferred income tax	47,540	13,133	–	–	60,673
Deferred acquisition costs	258,490	118,965	68,399	10,003	455,857
Financial assets carried at fair value	3,454,113	1,055,888	419,815	99,865	5,029,681
Reinsurance assets	1,982,352	247,268	142,926	84,029	2,456,575
Loans and receivables including insurance receivables	689,598	464,378	71,342	39,792	1,265,110
Current tax asset	1,019	10,135	2,424	–	13,578
Cash and cash equivalents	614,826	377,750	224,955	71,320	1,288,851
Total assets	7,090,640	2,511,909	935,134	308,622	10,846,305

	US Dollar $000	Sterling $000	Euro $000	Other $000	Total $000
Employee retirement benefit obligations	–	35,776	–	–	35,776
Deferred tax	–	–	–	–	–
Insurance liabilities	4,780,487	1,153,202	647,790	119,996	6,701,475
Financial liabilities	2,070	697,682	27	770	700,549
Current tax	8,460	–	1,847	–	10,307
Trade and other payables	687,625	264,770	83,478	45,207	1,081,080
Total liabilities	5,478,642	2,151,430	733,142	165,973	8,529,187
Total equity	1,611,998	360,479	201,992	142,649	2,317,118

3 Management of risk
3.2 Financial risk
(f) Currency risk continued

As at 31 December 2017 (restated)*	US Dollar $000	Sterling $000	Euro $000	Other $000	Total $000
Goodwill and intangible assets	16,643	167,068	–	2,327	186,038
Property, plant and equipment	5,584	54,600	4,097	1,347	65,628
Investments in associates	207	9,972	544	–	10,723
Deferred tax	45,788	6,863	811	–	53,462
Deferred acquisition costs	242,272	133,052	61,784	9,021	446,129
Financial assets carried at fair value	3,524,143	1,076,914	447,827	90,759	5,139,643
Reinsurance assets	1,583,031	162,352	56,502	31,370	1,833,255
Loans and receivables including insurance receivables	629,554	361,350	90,979	39,569	1,121,452
Current tax asset	–	5,682	34	–	5,716
Cash and cash equivalents	444,240	212,891	149,832	60,804	867,767
Total assets	6,491,462	2,190,744	812,410	235,197	9,729,813

	US Dollar $000	Sterling $000	Euro $000	Other $000	Total $000
Employee retirement benefit obligations	–	64,114	–	–	64,114
Deferred tax	–	–	–	–	–
Insurance liabilities	4,111,370	1,196,015	591,836	108,529	6,007,750
Financial liabilities	18,590	372,520	–	–	391,110
Current tax	–	–	9,384	72	9,456
Trade and other payables	542,170	239,607	60,935	46,290	889,002
Total liabilities	4,672,130	1,872,256	662,155	154,891	7,361,432
Total equity	1,819,332	318,488	150,255	80,306	2,368,381

*See note 2.1 for further details.

Sensitivity analysis
As at 31 December 2018, the Group used closing rates of exchange of $1:£0.79 and $1:€0.87 (2017: $1:£0.74 and $1:€0.84). The Group performs sensitivity analysis based on a 10% strengthening or weakening of US Dollar against the Pound Sterling and Euro.

This analysis assumes that all other variables, in particular interest rates, remain constant and that the underlying valuation of assets and liabilities in their base currency is unchanged. The process of deriving the undernoted estimates takes account of the linear retranslation movements of foreign currency monetary assets and liabilities together with the impact on the retranslation of those Group entities with non-US Dollar functional currency financial statements.

During the year, the Group transacted in a number of over-the-counter forward currency derivative contracts. The impact of these contracts on the sensitivity analysis is negligible.

As at 31 December	December 2018 effect on equity after tax $m	December 2018 effect on profit before tax $m	December 2017 effect on equity after tax $m	December 2017 effect on profit before tax $m
Strengthening of Pound Sterling	**52.2**	**9.0**	192.8	115.2
Weakening of Pound Sterling	**(42.7)**	**(7.4)**	(157.7)	(94.2)
Strengthening of Euro	**16.5**	**9.9**	11.5	12.5
Weakening of Euro	**(13.5)**	**(8.1)**	(9.4)	(10.3)

(g) Limitations of sensitivity analysis
The sensitivity information given in notes 3.2(a) to (f) demonstrates the estimated impact of a change in a major input assumption while other assumptions remain unchanged. In reality, there are normally significant levels of correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results. The same limitations exist in respect to the retirement benefit scheme sensitivities presented in note 27 to these financial statements. Furthermore, estimates of sensitivity may become less reliable in unusual market conditions such as instances when risk-free interest rates fall towards zero.

The sensitivity analysis does not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs. For example, the Group's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action.

3 Management of risk continued
3.3 Capital risk management

The Group's primary objectives when managing its capital position are:
- to safeguard its ability to continue as a going concern, so that it can continue to provide long-term growth and progressive dividend returns for shareholders;
- to provide an adequate return to the Group's shareholders by pricing its insurance products and services commensurately with the level of risk;
- to maintain an efficient cost of capital;
- to comply with all regulatory requirements by an appropriate margin;
- to maintain financial strength ratings of A in each of its insurance entities; and
- to settle policyholders' claims as they arise.

The Group sets the amount of capital required in its funding structure in proportion to risk. The Group then manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to obtain or maintain an optimal capital structure the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, assume debt, or sell assets to reduce debt.

The Group measures its capital requirements against its available capital. Available capital is defined by the Group as the total of net tangible asset value and subordinated debt.

The subordinated debt issued by the Group is hybrid in nature, which means it counts towards regulatory and rating agency capital requirements.

At 31 December 2018 available capital was $2,463 million (2017: $2,553 million), comprising net tangible asset value of $2,113 million (2017: $2,182 million) and subordinated debt of $350 million (2017: $371 million).

The Group can source additional funding from revolving credit and Letter of Credit (LOC) facilities. Standby funding from these sources comprised $800 million at 31 December 2018 (2017: $500 million), of which $50 million was utilised at 31 December 2018 (2017: $10 million).

The Board ensures that the use and allocation of capital are given a primary focus in all significant operational actions. With that in mind, the Group has developed and embedded capital modelling tools within its business. These join together short-term and long-term business plans and link divisional aspirations with the Group's overall strategy. The models provide the basis of the allocation of capital to different businesses and business lines, as well as the regulatory and rating agency capital processes.

Gearing

The Group currently utilises gearing as an additional source of funds to maximise the opportunities from strong markets and to reduce the risk profile of the business when the rating environment shows a weaker model for the more volatile business. The Group's gearing is obtained from a number of sources, including:
- Letter of Credit and revolving credit facility – the Group's main facility of $800 million may be drawn as cash (under a revolving credit facility), utilised as Letter of Credit or a combination thereof. This facility was increased to $800 million from $500 million in June 2018 by the Company's subsidiary Hiscox plc with the maximum cash portion increased to $800 million from $300 million. This enables the Group to utilise the Letter of Credit as Funds at Lloyd's to support underwriting on the 2018, 2019 and 2020 years of account. The facility can also be used to provide regulatory ancillary own funds within a number of the Group's insurance companies. The revolving credit facility has a maximum three-year contractual period for repayment. At 31 December 2018 $50 million was utilised by way of Letter of Credit to support the Funds at Lloyd's requirement and there were no cash drawings outstanding to support general trading activities (2017: $10 million and £nil respectively);
- £275 million of fixed-to-floating rate subordinated notes that are classified as Tier 2 debt. This was raised in November 2015 and matures in 2045. The debt is rated BBB- by S&P and Fitch;
- £275 million of fixed rate senior notes raised in March 2018 and maturing in 2022. The debt is rated BBB+ by S&P and Fitch;
- external Names – 27.4% of Syndicate 33's capacity is capitalised by third parties paying a profit share of approximately 20%;
- Syndicate 6104 at Lloyd's – with a capacity of £56 million for the 2019 year of account (2018 year of account: £56 million). This Syndicate is wholly backed by external members and takes pure years of account quota share of Syndicate 33's international property catastrophe reinsurance account;
- gearing quota shares – historically the Group has used reinsurance capital to fund its capital requirement for short-term expansions in the volume of business underwritten by the Syndicate; and
- qualifying quota shares – these are reinsurance arrangements that allow the Group to increase the amount of premium it writes.

Financial strength

The financial strength ratings of the Group's significant insurance company subsidiaries are outlined below:

	A.M. Best	Fitch	S&P
Hiscox Insurance Company Limited	A (Excellent)	A+	A (Strong)
Hiscox Insurance Company (Bermuda) Limited	A (Excellent)	A+	A (Strong)
Hiscox Insurance Company (Guernsey) Limited	A (Excellent)	A+	–
Hiscox Insurance Company Inc.	A (Excellent)	–	–
Hiscox Société Anonyme	–	–	A (Strong)

Syndicate 33 benefits from an A.M. Best rating of A (Excellent). In addition, the Syndicate also benefits from the Lloyd's ratings of A (Excellent) from A.M. Best, A+ (Strong) from S&P and AA- (Very strong) from Fitch.

Capital performance

The Group's main capital performance measure is the achieved return on equity (ROE). This marker best aligns the aspirations of employees and shareholders. As variable remuneration, the vesting of options and longer-term investment plans all relate directly to ROE, this concept is embedded in the workings and culture of the Group. The Group seeks to maintain its cost of capital levels and its debt to overall equity ratios in line with others in the non-life insurance industry.

Capital modelling and regulation

The capital requirements of an insurance group are determined by its exposure

3 Management of risk
3.3 Capital risk management
Capital modelling and regulation continued

to risk and the solvency criteria established by management and statutory regulations.

The Group's capital requirements are managed both centrally and at a regulated entity level. The assessed capital requirement for the business placed through Hiscox Insurance Company Limited, Hiscox Insurance Company (Bermuda) Limited, Hiscox Insurance Company (Guernsey) Limited, Hiscox Insurance Company Inc. and Hiscox Société Anonyme is driven by the level of resources necessary to maintain regulatory requirements.

The Group's regulatory capital is supervised by the Bermuda Monetary Authority (BMA). The Group had sufficient capital at all times throughout the year to meet the BMA's requirements. The BMA is planning to phase in changes between the 2019 and 2021 year-ends. The Group expect to maintain an appropriate margin of solvency after these changes have taken effect.

The Solvency II regime came into force in Europe on 1 January 2016. This requires insurance companies to calculate their capital requirements using either an internal model or a standard formula. Hiscox Insurance Company Limited and Hiscox Société Anonyme use the standard formula to calculate their regulatory capital requirements. Their risk profiles are sufficiently well represented by the standard formula not to warrant going through the internal model approval process. Hiscox's Lloyd's operations use the internal model that has been built to meet the requirements of the Solvency II regime. The model is concentrated specifically on the particular product lines, market conditions and risk appetite of each risk carrier.

For Syndicate 33 and Syndicate 3624, internal model results are uplifted by Lloyd's to the level of capital required to support its ratings. Capital models are used more widely across the Group to monitor exposure to key risk types, inform decision-making and measure ROE across different segments of the business. From the 2016 year end, the Group has been required to publish a financial condition report, as part of its regulatory filing with the BMA. This is a public document and sets out the financial performance and solvency position of the Group in accordance with the economic balance sheet return filed with the BMA. It is intended to provide the public with certain information to be able to make informed assessments about the Group. In the Group's other geographical territories, including the USA and Asia, its subsidiaries underwriting insurance business are required to operate within broadly similar risk-based externally imposed capital requirements when accepting business.

During the year the Group was in compliance with capital requirements imposed by regulators in each jurisdiction where the Group operates.

3.4 Tax risk
The Group is subject to income taxes levied by the various jurisdictions in which the Group operates, and the division of taxing rights between these jurisdictions results in the Group tax expense and effective rate of income tax disclosed in these financial statements. Due to the Group's operating model, there is an unquantifiable risk that this division of taxing rights could be altered materially, either by a change to the tax residence, or permanent establishment profile, of Hiscox Ltd or its principal subsidiaries; or due to the re-pricing or re-characterisation for tax purposes of transactions between members of the Group, under local transfer pricing or related tax legislation. The Group seeks to manage this risk by:
- maintaining appropriate internal policies and controls over its operations worldwide;
- monitoring compliance with these policies on an ongoing basis;
- adhering to internationally recognised best practice in determining the appropriate division of profits between taxing jurisdictions.
- taking additional advice and obtaining legal opinions from local third-party professionals with the necessary experience in the particular area.

The Group seeks to maintain an open dialogue with the relevant tax authorities and to resolve any issues arising promptly.

4 Operating segments
The Group's operating segment reporting follows the organisational structure and management's internal reporting systems, which form the basis for assessing the financial reporting performance of, and allocation of resource to each business segment. In 2018, the Group has reviewed the segmental presentation of financial information it requires to assess performance and allocate resources. It now considers that run-off portfolios where the Group has ceded all insurance risks to a third party should no longer be presented as part of the underwriting operations as these will not form part of the Group's assessment of the performance of the segment going forward and also will no longer generate returns for the Group. These run-off portfolios together with the reinsurance ceded are presented as part of the Corporate Centre segment. In line with the change in management's internal reporting, the segmental reporting has been updated accordingly. This change would also provide more meaningful views and trends of the underwriting performance of the business.

The Group's four primary business segments are identified as follows:
- **Hiscox Retail** brings together the results of Hiscox UK & Europe and Hiscox International being the USA, Special Risks and Asia retail business divisions. Hiscox UK & Europe underwrites European personal and commercial lines of business through Hiscox Insurance Company Limited, together with the fine art and non-US household insurance business written through Syndicate 33. In addition, Hiscox UK includes elements of specialty and international employees and officers' insurance written by Syndicate 3624 and Hiscox Europe excludes the kidnap and ransom business written by Hiscox Insurance Company Limited. Hiscox International comprises the specialty and fine art lines written through Hiscox Insurance Company (Guernsey) Limited, and the motor business written via DirectAsia, together with US commercial, property and specialty business written by Syndicate 3624 and Hiscox Insurance Company Inc. via the Hiscox USA business division. It also includes the European kidnap and ransom business written by Hiscox Insurance Company Limited and Syndicate 33.
- **Hiscox London Market** comprises the internationally traded insurance business written by the Group's London-based underwriters via Syndicate 33, including lines in property, marine and energy, casualty and other specialty insurance lines, excluding the kidnap and ransom business. In addition, the segment includes elements of business written by Syndicate 3624 being auto physical damage and aviation business.

4 Operating segments continued

- **Hiscox Re & ILS** is the reinsurance division of the Hiscox Group, combining the underwriting platforms in Bermuda and London. The segment comprises the performance of Hiscox Insurance Company (Bermuda) Limited, excluding the internal quota share arrangements, with the reinsurance contracts written by Syndicate 33. In addition, the healthcare and casualty reinsurance contracts written in the Bermuda hub on Syndicate capacity are included. The segment also includes the performance and fee income from the ILS funds, along with the gains and losses made as a result of the Group's investment in the funds.
- **Corporate Centre** comprises the investment return, finance costs and administrative costs associated with Group management activities. Corporate Centre also includes the majority of foreign currency items on economic hedges and intragroup borrowings. These relate to certain foreign currency items on economic hedges and intragroup borrowings. In addition, from 1 January 2018, the segment includes results from run-off portfolios where the Group has ceded all insurance risks to a third-party reinsurer. Corporate Centre forms a reportable segment due to its investment activities which earn significant external returns.

All amounts reported below represent transactions with external parties only. In the normal course of trade, the Group's entities enter into various reinsurance arrangements with one another. The related results of these transactions are eliminated on consolidation and are not included within the results of the segments. This is consistent with the information used by the chief operating decision-maker when evaluating the results of the Group. Performance is measured based on each reportable segment's profit before tax.

(a) Profit before tax by segment

	Year to 31 December 2018					Year to 31 December 2017 (restated)*				
	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre† $000	Total $000	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000
Gross premiums written	2,087,117	877,697	812,010	1,517	3,778,341	1,835,428	749,793	700,800	–	3,286,021
Net premiums written	1,874,483	522,948	241,464	(57,409)	2,581,486	1,674,238	484,945	243,816	–	2,402,999
Net premiums earned	1,821,855	551,764	257,429	(57,409)	2,573,639	1,585,289	561,572	269,347	–	2,416,208
Investment result	9,515	13,307	12,902	2,377	38,101	29,361	14,509	27,942	32,938	104,750
Other income	23,787	9,745	13,135	118	46,785	35,351	13,908	4,350	470	54,079
Total income	1,855,157	574,816	283,466	(54,914)	2,658,525	1,650,001	589,989	301,639	33,408	2,575,037
Claims and claim adjustment expenses, net of reinsurance	(812,124)	(253,273)	(217,952)	57,520	(1,225,829)	(721,851)	(400,229)	(188,836)	–	(1,310,916)
Expenses for the acquisition of insurance contracts	(459,326)	(164,556)	(17,401)	(388)	(641,671)	(401,070)	(159,823)	(27,037)	–	(587,930)
Operational expenses	(448,516)	(75,502)	(58,390)	(23,310)	(605,718)	(384,685)	(61,469)	(53,294)	(29,525)	(528,973)
Foreign exchange gains/(losses)	1,173	(2,619)	(11,608)	(634)	(13,688)	(530)	(15,174)	(5,253)	(59,933)	(80,890)
Total expenses	(1,718,793)	(495,950)	(305,351)	33,188	(2,486,906)	(1,508,136)	(636,695)	(274,420)	(89,458)	(2,508,709)
Results of operating activities	136,364	78,866	(21,885)	(21,726)	171,619	141,865	(46,706)	27,219	(56,050)	66,328
Finance costs	(201)	(629)	(1,315)	(32,528)	(34,673)	(10)	–	(1,716)	(25,169)	(26,895)
Share of (loss)/profit of associates after tax	(206)	–	–	635	429	(247)	–	–	506	259
Profit/(loss) before tax	135,957	78,237	(23,200)	(53,619)	137,375	141,608	(46,706)	25,503	(80,713)	39,692
Profit/(loss) before tax and foreign exchange gains/(losses)	134,784	80,856	(11,592)	(52,985)	151,063	142,138	(31,532)	30,756	(20,780)	120,582

*See note 2.1 for further details.
†Includes a run-off casualty portfolio following the completion of a loss portfolio transfer reinsurance treaty effective from 2018 ceding any future payments on losses arising from claims developments related to policies written from 2010 to 2016, with premiums earned of $(57.4) million and claims adjustment expenses net of reinsurance of $57.5 million.

4 Operating segments

(a) Profit before tax by segment continued

The following charges are included within the consolidated income statement:

	Year to 31 December 2018					Year to 31 December 2017 (restated)*				
	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000
Depreciation	6,790	1,050	472	396	8,708	5,004	974	759	418	7,155
Amortisation of intangible assets	17,896	5,098	1,378	104	24,476	14,251	3,821	599	124	18,795
Impairment of intangible assets	–	–	–	–	–	1,958	–	–	–	1,958
Total	24,686	6,148	1,850	500	33,184	21,213	4,795	1,358	542	27,908

*See note 2.1 for further details.

The Group's wholly owned subsidiary, Hiscox Syndicates Limited, oversees the operation of Syndicate 33 at Lloyd's. The Group's percentage participation in Syndicate 33 can fluctuate from year-to-year and, consequently, presentation of the results at the 100% level removes any distortions arising therefrom.

	Year to 31 December 2018					Year to 31 December 2017 (restated)*				
100% ratio analysis	Hiscox Retail	Hiscox London Market	Hiscox Re & ILS	Corporate Centre	Total	Hiscox Retail	Hiscox London Market	Hiscox Re & ILS	Corporate Centre	Total
Claims ratio (%)	43.8	46.0	83.8	–	48.5	45.2	70.1	71.0	–	54.9
Expense ratio (%)	49.8	43.0	28.7	–	45.9	49.3	38.6	27.9	–	43.9
Combined ratio excluding foreign exchange impact (%)	93.6	89.0	112.5	–	94.4	94.5	108.7	98.9	–	98.8
Foreign exchange impact (%)	–	0.3	4.4	–	0.5	0.1	2.9	2.4	–	1.1
Combined ratio (%)	93.6	89.3	116.9	–	94.9	94.6	111.6	101.3	–	99.9

*See note 2.1 for further details.

The claims ratio is calculated as claims and claim adjustment expenses, net of reinsurance, as a proportion of net premiums earned. The expense ratio is calculated as the total of expenses for the acquisition of insurance contracts and operational expenses, including profit-related pay, as a proportion of net premiums earned. The foreign exchange impact ratio is calculated as the foreign exchange gains or losses as a proportion of net premiums earned. The combined ratio is the total of the claims, expenses and foreign exchange impact ratios. All ratios are calculated using the 100% results and excludes a run-off portfolio, where the Group has ceded all insurance risks to a third party reinsurer, included within Corporate Centre.

Costs allocated to the Corporate Centre are non-underwriting related costs and are not included within the combined ratio.
The impact on profit before tax of a 1% change in each component of the segmental combined ratios is shown in the following table. Any further ratio change is linear in nature.

	Year to 31 December 2018			Year to 31 December 2017 (restated)*		
	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000
At 100% level (note 4b) 1% change in claims or expense ratio	18,630	7,194	2,981	16,622	7,037	3,142
At Group level 1% change in claims or expense ratio	18,219	5,518	2,574	15,853	5,616	2,693

*See note 2.1 for further details.

4 Operating segments continued

(b) 100% operating result by segment

	Year to 31 December 2018					Year to 31 December 2017 (restated)*				
	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000
Gross premiums written	2,134,098	1,194,227	894,024	1,517	4,223,866	1,878,742	976,839	796,712	–	3,652,293
Net premiums written	1,913,765	710,790	282,018	(57,409)	2,849,164	1,713,630	621,985	288,998	–	2,624,613
Net premiums earned	1,862,975	719,441	298,137	(57,409)	2,823,144	1,622,173	703,657	314,205	–	2,640,035
Investment result	9,992	17,052	15,192	2,377	44,613	30,182	18,928	29,189	32,938	111,237
Other income	20,467	9,846	9,143	118	39,574	30,739	3,509	2,494	470	37,212
Claims and claim adjustment expenses, net of reinsurance	(816,109)	(330,924)	(249,797)	57,520	(1,339,310)	(734,160)	(493,201)	(222,953)	–	(1,450,314)
Expenses for the acquisition of insurance contracts	(475,623)	(213,872)	(19,535)	(388)	(709,418)	(413,145)	(197,629)	(28,488)	–	(639,262)
Operational expenses	(451,864)	(95,257)	(65,998)	(17,700)	(630,819)	(386,080)	(73,882)	(59,264)	(29,525)	(548,751)
Foreign exchange gains/(losses)	295	(2,687)	(13,184)	(633)	(16,209)	(1,120)	(20,531)	(7,535)	(59,933)	(89,119)
Results of operating activities	150,133	103,599	(26,042)	(16,115)	211,575	148,589	(59,149)	27,648	(56,050)	61,038

*See note 2.1 for further details.

Segment results at the 100% level presented above differ from those presented at the Group's share at note 4(a) solely as a result of the Group not owning 100% of the capacity of Syndicate 33 at Lloyd's.

(c) Geographical information

The Group's operational segments underwrite business domestically in Bermuda and from locations in the UK and Ireland, the US, Guernsey, France, Germany, Belgium, The Netherlands, Spain, Portugal, Singapore and Thailand.

The following table provides an analysis of the Group's gross premium revenues earned by material geographical location from external parties:

	Year to 31 December 2018					Year to 31 December 2017 (restated)*				
Gross premium revenues earned from external parties	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000	Hiscox Retail $000	Hiscox London Market $000	Hiscox Re & ILS $000	Corporate Centre $000	Total $000
UK & Ireland	701,342	21,339	12,354	1,517	736,552	622,173	22,159	10,530	–	654,862
Europe	416,321	38,963	17,101	–	472,385	350,469	55,802	12,875	–	419,146
United States	814,942	683,255	533,567	–	2,031,764	664,081	635,792	511,291	–	1,811,164
Rest of world	78,751	150,545	229,805	–	459,101	83,311	148,296	179,186	–	410,793
	2,011,356	894,102	792,827	1,517	3,699,802	1,720,034	862,049	713,882	–	3,295,965

The Group's largest external policyholder contributed less than 2% of total gross Group premium revenues earned and the details thereof are not disclosed on the grounds of materiality.

The following table provides an analysis of the Group's non-current assets by material geographical location excluding financial instruments, deferred tax assets, post-employment benefit assets, and rights arising under insurance contracts:

Non-current assets	2018 total $000	2017 total (restated)* $000
UK & Ireland	215,582	231,665
Europe	4,790	4,883
United States	51,998	22,168
Rest of world	3,611	3,685
	275,981	262,401

*See note 2.1 for further details.

5 Net asset value per share

	2018		2017 (restated)*	
	Net asset value (total equity) $000	Net asset value per share cents	Net asset value (total equity) $000	Net asset value per share cents
Net asset value	2,317,118	819.1	2,368,381	835.1
Net tangible asset value	2,112,518	746.8	2,182,343	769.5

*See note 2.1 for further details.

The net asset value per share is based on 282,886,319 shares (2017: 283,600,709 shares), being the shares in issue at 31 December 2018, less those held in treasury and those held by the Group Employee Benefit Trust.

Net tangible assets comprise total equity excluding intangible assets. The net asset value per share expressed in pence is 643.1p (31 December 2017: 618.6p).

6 Return on equity

	2018 $000	2017 (restated)* $000
Profit for the year (all attributable to owners of the Company)	127,999	33,904
Opening total equity	2,368,381	2,254,820
Adjusted for the time-weighted impact of capital distributions and issuance of shares	(83,664)	(43,525)
Adjusted opening total equity	2,284,717	2,211,295
Return on equity (%)	5.6	1.5

*See note 2.1 for further details.

The return on equity is calculated by using profit for the period divided by the adjusted opening total equity. The adjusted opening total equity represents the equity on 1 January of the relevant year as adjusted for time weighted aspects of capital distributions and issuing of shares or treasury share purchases during the period. The time weighted positions are calculated on a daily basis with reference to the proportion of time from the transaction to the end of the period.

7 Investment result

The total result for the Group before taxation comprises:

	Note	2018 $000	2017 (restated)* $000
Investment income including interest receivable		102,955	81,590
Net realised losses on financial investments at fair value through profit or loss		(25,397)	(5,130)
Net fair value (losses)/gains on financial investments at fair value through profit or loss		(35,070)	36,055
Investment result – financial assets	8	42,488	112,515
Net fair value gains/(losses) on derivative financial instruments	19	1,280	(1,695)
Investment expenses		(5,667)	(6,070)
Total result		38,101	104,750

*See note 2.1 for further details.

8 Analysis of return on financial investments

(a) The weighted average return on financial investments for the year by currency, based on monthly asset values, was:

	2018 %	2017 (restated)* %
US Dollar	1.1	2.1
Sterling	(0.5)	2.6
Other	0.3	–

*See note 2.1 for further details.

8 Analysis of return on financial investments continued

(b) Investment return

	2018 Return $000	2018 Yield %	2017 (restated)* Return $000	2017 (restated)* Yield %
Debt and fixed income securities	57,507	1.3	54,241	1.2
Equities and units in unit trusts	(27,513)	(6.2)	53,434	12.9
Deposits with credit institutions/cash and cash equivalents	12,494	0.8	4,840	0.5
Investment result – financial assets	42,488	0.7	112,515	2.0

*See note 2.1 for further details.

9 Other income and operational expenses

	2018 $000	2017 (restated)* $000
Agency-related income	27,061	16,176
Profit commission	6,959	11,746
Other underwriting loss	(3,362)	(7,360)
Other income†	16,127	33,517
Other income	46,785	54,079
Wages and salaries	212,377	168,234
Social security cost	32,689	30,022
Pension cost – defined contribution	14,640	12,765
Pension cost – defined benefit	2,188	2,263
Share-based payments	(3,638)	32,465
Marketing expenses	69,711	69,097
Depreciation, amortisation and impairment	33,184	27,908
Other expenses	244,567	186,219
Operational expenses	605,718	528,973

*See note 2.1 for further details.
†Comparative includes results of the sale of a subsidiary and an associate in 2017.

Agency-related income relates to commission received from a non-Group insurer by an insurance intermediary ('agency') for placement services and in limited cases claims handling services. Commission income associated with the placement services are recognised at the point in time when the agency has satisfied its performance obligation. That is when the terms of the insurance policy have been agreed contractually by the insurer and policyholder and the insurer has a present right to payment from the policyholder. Where the agency also provides the insurer with claims handling services, the commission income associated with these services are recognised over time in line with the terms of the contractual arrangements.

Profit-commission income attributed to non-insurance entities, for example, Lloyd's managing agent and ILS investment managers are determined based on a best estimate of the variable consideration. The income is recognised to the extent that it is highly probable that it will not be subject to significant reversal.

Other underwriting income represents results from the insurance-linked securities managed by the Group and other income includes management fees which are recognised when the investment management services are rendered to the ILS funds.

Wages and salaries have been shown net of transfers to acquisition and claims expenses.

Other expenses include, but are not limited to, legal and professional costs, computer costs, contractor-based costs and property costs. None of the items are individually material.

10 Finance costs

	Note	2018 $000	2017 (restated)* $000
Interest charge associated with long-term debt	17	28,360	21,713
Interest and expenses associated with bank borrowing facilities		2,485	3,435
Interest and charges associated with Letters of Credit	30	3,199	909
Interest charges on experience account		629	838
Finance costs		34,673	26,895

*See note 2.1 for further details.

11 Auditor's remuneration

Fees payable to the Group's main external auditor, PwC, its member firms and its associates (exclusive of VAT) include the following amounts recorded in the consolidated income statement:

Group	2018 $000	2017 (restated)* $000
Amounts receivable by the auditor and its associates in respect of:		
The auditing of the accounts of the Group and its subsidiaries	**2,705**	2,493
All audit-related assurance services	**359**	266
All other non-audit services	**168**	257
	3,232	3,016

*See note 2.1 for further details.

The full audit fee payable for the Syndicate 33 audit has been included above, although an element of this is borne by the third-party participants in the Syndicate.

12 Goodwill and intangible assets

	Goodwill $000	Syndicate capacity $000	State authorisation licences $000	Software and development costs $000	Other $000	Total $000
At 1 January 2017 (restated)*						
Cost	12,605	30,386	7,822	136,637	55,485	242,935
Accumulated amortisation and impairment	(3,215)	–	–	(62,348)	(23,954)	(89,517)
Net book amount	9,390	30,386	7,822	74,289	31,531	153,418
Year ended 31 December 2017 (restated)*						
Opening net book amount	9,390	30,386	7,822	74,289	31,531	153,418
Additions	–	–	–	34,085	7,081	41,166
Amortisation charges	–	–	–	(13,832)	(4,963)	(18,795)
Impairment	(1,605)	–	–	–	(353)	(1,958)
Foreign exchange movements	756	2,696	694	5,515	2,546	12,207
Closing net book amount	8,541	33,082	8,516	100,057	35,842	186,038
At 31 December 2017 (restated)*						
Cost	13,723	33,082	8,516	182,292	67,488	305,101
Accumulated amortisation and impairment	(5,182)	–	–	(82,235)	(31,646)	(119,063)
Net book amount	8,541	33,082	8,516	100,057	35,842	186,038
Year ended 31 December 2018						
Opening net book amount	**8,541**	**33,082**	**8,516**	**100,057**	**35,842**	**186,038**
Additions	**–**	**–**	**–**	**51,532**	**–**	**51,532**
Amortisation charges	**–**	**–**	**–**	**(19,734)**	**(4,742)**	**(24,476)**
Impairment	**–**	**–**	**–**	**–**	**–**	**–**
Foreign exchange movements	**(115)**	**–**	**–**	**(7,615)**	**(764)**	**(8,494)**
Closing net book amount	**8,426**	**33,082**	**8,516**	**124,240**	**30,336**	**204,600**
At 31 December 2018						
Cost	**13,608**	**33,082**	**8,516**	**220,684**	**65,486**	**341,376**
Accumulated amortisation and impairment	**(5,182)**	**–**	**–**	**(96,444)**	**(35,150)**	**(136,776)**
Net book amount	**8,426**	**33,082**	**8,516**	**124,240**	**30,336**	**204,600**

*See note 2.1 for further details.

Goodwill

Goodwill is allocated to the Group's cash-generating units (CGUs) identified according to the smallest identifiable unit to which cash flows are generated. $7,398,000 (2017: $7,398,000) is allocated to the Lloyd's corporate member entity CGU and $1,028,000 (2017: $1,143,000) is allocated to the CGUs within the Hiscox Retail business segment. Goodwill is considered to have an indefinite life and as such is tested annually for impairment based on the recoverable amount which is considered to be the higher of the fair value less cost to sell or value in use.

12 Goodwill and intangible assets

Goodwill continued

Value in use is considered to be the best indication of the recoverable amount for goodwill. Value in use calculations are performed using cash flow projections based on financial forecasts covering a five-year period. A discount factor, based on a weighted average cost of capital (WACC) for the Group of 7.0% (2017: 6.7%), has been applied to the projections to determine the net present value. The outcome of the value in use calculation is measured against the carrying value of the asset and, where the carrying value is in excess of the value in use, the asset is written down to this amount.

In 2017, the $1,605,000 impairment recognised in the year for goodwill is included in operational expenses in the consolidated income statement. There was no impairment in 2018.

Intangible assets

All intangible assets have a finite useful life except for the Syndicate capacity and US state authorisation licences.

(a) Syndicate capacity

The cost of purchasing the Group's participation in the Lloyd's insurance syndicates is not amortised but is tested annually for impairment and is carried at cost less accumulated impairment losses. Having considered the future prospects of the London insurance market, the Board believes that the Group's ownership of Syndicate capacity will provide economic benefits over an indefinite number of future periods. This assumption is reviewed annually to determine whether the asset continues to have an indefinite life.

The Group's intangible asset relating to Syndicate capacity has been allocated, for impairment testing purposes, to one individual CGU, being the active Lloyd's corporate member entity. The asset is tested annually for impairment based on its recoverable amount which is considered to be the higher of the asset's fair value less costs to sell or its value in use. The fair value of Syndicate capacity can be determined from the Lloyd's of London Syndicate capacity auctions. Based on the average open market price witnessed in the recent autumn 2018 auction, the carrying value of Syndicate capacity recognised on the balance sheet is significantly below the market price.

(b) US state authorisation licences

As part of a business combination in 2007, the Group acquired insurance authorisation licences for 50 US states. This intangible asset has been allocated for impairment testing purposes to one individual CGU, being the Group's North American underwriting business.

The asset is not amortised, as the Group considers that economic benefits will accrue to the Group over an indefinite number of future periods due to the stability of the US insurance market. This assumption is reviewed annually to determine whether the asset continues to have an indefinite life.

The licences are tested annually for impairment, and accumulated impairment losses are deducted from the historical cost. The carrying value of this asset is tested for impairment based on its value in use. The value in use is calculated using a projected cash flow based on business plans approved by management and discounted at the WACC rate. Key assumptions include new business growth, retention rates, market cycle and claims inflation. The results of the test show there is no impairment.

(c) Software and development costs

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring into use the specific software. These costs are amortised over the expected useful life of the software of between three and ten years on a straight-line basis.

Internally developed computer software is only capitalised when it is probable that the expected future economic benefits that are attributable to the asset will flow to the Group and the cost of the asset can be measured reliably. Amortisation of internally developed computer software begins when the software is available for use and is allocated on a straight-line basis over the expected useful life of the asset.

The useful life of the asset is reviewed annually and, if different from previous estimates, is changed accordingly with the change being accounted for as a change in accounting estimates in accordance with IAS 8.

The carrying value of software and development costs is reviewed for impairment on an ongoing basis by reference to the stage and expectation of a project. Additionally, at the end of each reporting period, the Group reviews the positions for any indication of impairment, and as a result of this no impairment was provided for (2017: $nil).

At 31 December 2018 there were $37,502,000 of assets under development on which amortisation has yet to be charged (2017: $24,735,000).

The assets are expected to be recovered or settled more than 12 months after the reporting date and as such are considered to be non-current.

12 Goodwill and intangible assets continued

d) Rights to customer contractual relationships (included in other)

Costs directly attributable to securing the intangible rights to customer contractual relationships are recognised as an intangible asset where they can be identified separately and measured reliably and it is probable that they will be recovered by directly related future profits. These costs are amortised on a straight-line basis over the useful economic life which is deemed to be ten years and are carried at cost less accumulated amortisation and impairment losses.

At the end of each reporting period an assessment is made on whether there is any indication that customer contractual relationships may be impaired. Where indications of impairment are identified, the carrying value is tested for impairment based on the recoverable amount which is considered to be the higher of the fair value less costs to sell or value in use. The asset's value in use is considered to be the best indication of its recoverable amount. Value in use is calculated using the same method as described above for goodwill and the same discount rate used. The results of this test led to no impairment being recognised (2017: $353,000).

13 Property, plant and equipment

	Land and buildings $000	Leasehold improvements $000	Vehicles $000	Furniture fittings and equipment and art $000	Total $000
At 1 January 2017 (restated)*					
Cost	28,364	10,601	181	57,897	97,043
Accumulated depreciation	(1,738)	(6,444)	(83)	(28,731)	(36,996)
Net book amount	26,626	4,157	98	29,166	60,047
Year ended 31 December 2017 (restated)*					
Opening net book amount	26,626	4,157	98	29,166	60,047
Additions	–	1,311	32	7,316	8,659
Disposals	–	(107)	(70)	(297)	(474)
Depreciation charge	(1,188)	(1,427)	(36)	(4,504)	(7,155)
Foreign exchange movements	2,305	24	7	2,215	4,551
Closing net book amount	27,743	3,958	31	33,896	65,628
At 31 December 2017 (restated)*					
Cost	30,880	11,781	47	69,288	111,996
Accumulated depreciation	(3,137)	(7,823)	(16)	(35,392)	(46,368)
Net book amount	27,743	3,958	31	33,896	65,628
Year ended 31 December 2018					
Opening net book amount	**27,743**	**3,958**	**31**	**33,896**	**65,628**
Additions	**–**	**508**	**–**	**7,362**	**7,870**
Disposals	**–**	**–**	**–**	**(159)**	**(159)**
Depreciation charge	**(1,233)**	**(1,163)**	**(12)**	**(6,300)**	**(8,708)**
Transfers	**95**	**–**	**–**	**(95)**	**–**
Foreign exchange movements	**(1,513)**	**(4)**	**(2)**	**(1,654)**	**(3,173)**
Closing net book amount	**25,092**	**3,299**	**17**	**33,050**	**61,458**
At 31 December 2018					
Cost	**29,227**	**12,031**	**46**	**72,958**	**114,262**
Accumulated depreciation	**(4,135)**	**(8,732)**	**(29)**	**(39,908)**	**(52,804)**
Net book amount	**25,092**	**3,299**	**17**	**33,050**	**61,458**

*See note 2.1 for further details.

The Group's land and buildings assets relate to freehold property in the UK. There was no impairment charge during the year (2017: $nil). Assets with a net book value of $nil were held under finance leases (2017: $nil).

The assets are expected to be recovered or settled more than 12 months after the reporting date and as such are considered to be non-current.

14 Subsidiaries, associates and interests in other entities

This note provides details of the Syndicates and Special Purpose Insurers (SPI) managed by the Group, the acquisition and disposal of subsidiaries and associates during the year and investments in associates.

(a) Subsidiaries

Hiscox Dedicated Corporate Member Limited (HDCM) underwrites as a corporate member of Lloyd's on the main Syndicates managed by Hiscox Syndicates Limited (the main managed Syndicates numbered 33 and 3624).

As at 31 December 2018, HDCM owned 72.6% of Syndicate 33 (2017: 72.6%), and 100% of Syndicate 3624 (2017: 100%). In view of the several, but not joint liability of, underwriting members at Lloyd's for the transactions of Syndicates in which they participate, the Group's attributable share of the transactions, assets and liabilities of these Syndicates has been included in the financial statements. The Group manages the underwriting of, but does not participate as a member of, Syndicate 6104 at Lloyd's which provides reinsurance to Syndicate 33 on a normal commercial basis. Consequently, aside from the receipt of managing agency fees, defined profit commissions as appropriate and interest arising on effective assets included within the experience account, the Group has no share in the assets, liabilities or transactions of Syndicate 6104. The position and performance of that Syndicate is therefore not included in the Group's financial statements.

(b) Special Purpose Insurers

The Kiskadee Diversified Fund and Kiskadee Select Fund (the Funds) were launched in 2014 to provide investment opportunities to institutional investors in property catastrophe reinsurance and insurance-linked strategies. The Funds are managed by Hiscox Re Insurance Linked Strategies Ltd (formerly known as Kiskadee Investment Managers Ltd) which is a wholly owned subsidiary of the Group. The majority of the Funds' exposures to reinsurance risk are fronted by the Group into two Bermuda Licensed Special Purpose Insurers (SPI), Kiskadee Reinsurance 1 Ltd and Kiskadee Reinsurance 2 Ltd which have been collateralised by the Funds.

Following a significant inflow of capital from third-party investors during 2015, the Group determined that it no longer met the criteria for consolidation of the Funds and SPIs from 1 July 2015 and deconsolidated them.

As at 31 December 2018, the Group recognised a financial asset at fair value of $55.2 million (2017: $49.9 million) in relation to its investment in the Funds (note 17). In assessing the maximum exposure to loss from its interest in the Funds and SPIs, the Group has determined it is no greater than the fair value recognised as at the balance sheet date. The total size of the funds were $951 million at 31 December 2018 (2017: $818 million). In addition to the return on the financial asset, the Group also receives fee income through Hiscox Re Insurance Linked Strategies Ltd and Hiscox Insurance Company (Bermuda) Ltd, both wholly owned subsidiaries, under normal commercial terms.

The Group is exposed to credit risk associated with reinsurance recoverables on risks fronted for the SPIs. Note 3.2(d) discusses how the Group manages credit risk associated with reinsurance assets. The operations of the Funds and SPIs are financed through the issuance of preference shares to external investors. The Group does not intend to provide any further financial support to the Funds or SPIs.

14 Subsidiaries, associates and interests in other entities continued

(c) Investments in associates

Year ended 31 December	2018 $000	2017 (restated)* $000
At beginning of year	10,723	17,155
Disposals during the year	–	(7,549)
Distributions received	(356)	(646)
Net profit from investments in associates	429	259
Foreign exchange movements	(874)	1,504
At end of year	**9,922**	10,723

*See note 2.1 for further details.

The Group's interests in its principal associates, all of which are unlisted, were as follows:

		100% results			
	% interest held at 31 December	Assets $000	Liabilities $000	Revenues $000	Profit after tax $000
2018					
Associates incorporated in the UK and USA	from 17% to 35%	16,939	11,779	16,319	1,332
Associates incorporated in Europe	from 10% to 26%	2,833	1,336	2,641	804
Total at the end of 2018		**19,772**	**13,115**	**18,960**	**2,136**

		100% results			
	% interest held at 31 December	Assets $000	Liabilities $000	Revenues $000	Profit after tax $000
2017 (restated)*					
Associates incorporated in the UK	from 17% to 35%	17,688	13,029	19,398	1,422
Associates incorporated in Europe	from 10% to 26%	3,629	2,434	2,728	858
Total at the end of 2017		21,317	15,463	22,126	2,280

*See note 2.1 for further details.

The equity interests held by the Group in respect of associates do not have quoted market prices and are not traded regularly in any active recognised market. The associates concerned have no material impact on the results or assets of the Group.

The assets are expected to be recovered or settled more than 12 months after the reporting date and as such are considered to be non-current.

(d) Disposals

On 1 May 2017, the Group disposed of its subsidiary Blue Hill Specialty Insurance Company Inc. and on 18 September 2017, the Group completed the sale of its investment in Lark (2012) Limited.

As a result of the disposals, the Group has derecognised the assets and liabilities relating to the companies. Below is a table disclosing the impact to the consolidated financial statement following the disposal.

	Note	2017 (restated)* $000
Total assets no longer recognised in the consolidated balance sheet		(33,151)
Total currency translation reserve no longer recognised in the consolidated balance sheet		1
Cash received on disposal		50,921
Profit recognised in the consolidated income statement	9	17,771

*See note 2.1 for further details.

15 Deferred acquisition costs

	2018			2017 (restated)*		
	Gross $000	Reinsurance $000	Net $000	Gross $000	Reinsurance $000	Net $000
Balance deferred at 1 January	446,129	(91,805)	354,324	429,777	(82,684)	347,093
Acquisition costs incurred in relation to insurance contracts written	898,113	(255,876)	642,237	796,829	(217,092)	579,737
Acquisition costs expensed to the income statement	(881,974)	240,303	(641,671)	(798,809)	210,879	(587,930)
Foreign exchange and other adjustments	(6,411)	620	(5,791)	18,332	(2,908)	15,424
Balance deferred at 31 December	455,857	(106,758)	349,099	446,129	(91,805)	354,324

The deferred amount of insurance contract acquisition costs attributable to reinsurers of $106,758,000 (2017: $91,805,000) is not eligible for offset against the gross balance sheet asset and is included separately within trade and other payables (note 24).

The net amounts expected to be recovered before and after one year are estimated as follows:

	2018 $000	2017 (restated)* $000
Within one year	314,675	321,524
After one year	34,424	32,800
	349,099	354,324

*See note 2.1 for further details.

16 Reinsurance assets

	Note	2018 $000	2017 (restated)* $000
Reinsurers' share of insurance liabilities		2,457,349	1,834,039
Provision for non-recovery and impairment		(774)	(784)
Reinsurance assets	23	2,456,575	1,833,255

The amounts expected to be recovered before and after one year, based on historical experience, are estimated as follows:

	2018 $000	2017 (restated)* $000
Within one year	1,277,862	925,805
After one year	1,178,713	907,450
	2,456,575	1,833,255

*See note 2.1 for further details.

Amounts due from reinsurers in respect of outstanding premiums and claims already paid by the Group are included in loans and receivables (note 18). The Group recognised a gain during the year of $10,000 (2017: gain of $19,000) in respect of previously impaired balances.

17 Financial assets and liabilities

Financial assets designated at fair value through profit or loss are measured at their bid price values, with all changes from one accounting period to the next being recorded through the income statement.

	Note	2018 $000	2017 (restated)* $000
Debt and fixed income securities		4,574,629	4,630,828
Equities and shares in unit trusts		398,055	451,305
Deposits with credit institutions		364	7,182
Total investments		4,973,048	5,089,315
Insurance-linked fund		55,182	49,918
Derivative financial instruments	19	1,451	410
Total financial assets carried at fair value		5,029,681	5,139,643

The effective maturity of the debt and fixed income securities due within and after one year are as follows:

	2018 $000	2017 (restated)* $000
Within one year	1,298,228	1,075,393
After one year	3,276,401	3,555,435
	4,574,629	4,630,828

*See note 2.1 for further details.

Equities, shares in unit trusts and insurance-linked securities do not have any maturity dates. The effective maturity of all other financial assets are due within one year.

An analysis of the credit risk and contractual maturity profiles of the Group's financial instruments is given in notes 3.2(d) and 3.2(e).

	Note	2018 $000	2017 (restated)* $000
Amounts owed to credit institutions		–	18,446
Derivative financial instruments	19	1,079	163
Total financial liabilities carried at fair value		1,079	18,609

	2018 $000	2017 (restated)* $000
Long-term debt	697,120	370,071
Accrued interest on long-term debt	2,350	2,430
Total financial liabilities carried at amortised cost	699,470	372,501

*See note 2.1 for further details.

All of the financial liabilities carried at fair value are due within one year. The amounts owed to credit institutions relate to outstanding investment trades in trust funds that are not available for offset against the same counterparty under cash and cash equivalents. These positions would be rated A had they have been recorded under cash and cash equivalents. The long-term debt is due after one year, with its accrued interest due within one year.

On 24 November 2015, the Group issued £275.0 million 6.125% fixed-to-floating rate callable subordinated notes due 2045, with a first call date of 2025.

The notes bear interest from, and including, 24 November 2015 at a fixed rate of 6.125% per annum annually in arrears starting 24 November 2016 up until the first call date in November 2025 and thereafter at a floating rate of interest equal to three-month LIBOR plus 5.076% payable quarterly in arrears on each floating interest payment date.

On 25 November 2015 the notes were admitted for trading on the London Stock Exchange's regulated market. The notes were rated BBB- by S&P as well as by Fitch.

On 14 March 2018, the Group issued £275.0 million 2% notes due December 2022. The notes will be redeemed on the maturity date at their principal amount together with accrued interest.

The notes bear interest from, and including, 14 March 2018 at a fixed rate of 2% per annum annually in arrears starting 14 December 2018 until maturity on 14 December 2022.

On 14 March 2018, the notes were admitted for trading on the Luxembourg Stock Exchange's Euro MTF. The notes were rated BBB+ by S&P, as well as by Fitch.

17 Financial assets and liabilities continued

The fair value of the long-term debt is estimated at $706.3 million (2017: $428.5 million). The fair value measurement is classified within Level 1 of the fair value hierarchy. The fair value is estimated by reference to the actively traded value on the stock exchanges.

The increase in the carrying value of the long-term debt and accrued interest during the year comprises new debt issued at $380.3 million, the amortisation of the difference between the net proceeds received and the redemption amounts of $0.6 million (2017: $0.1 million) less exchange movements of $53.9 million (2017: plus exchange movements of $30.4 million).

Note 10 includes details of the interest expense for the year included in financing costs.

Investments at 31 December are denominated in the following currencies at their fair value:

	2018 $000	2017 (restated)* $000
Debt and fixed income securities		
US Dollars	3,161,586	3,227,118
Sterling	895,172	868,839
Euro and other currencies	517,871	534,871
	4,574,629	4,630,828
Equities and shares in unit trusts		
US Dollars	237,339	246,697
Sterling	160,716	204,608
Euro and other currencies	–	–
	398,055	451,305
Deposits with credit institutions		
US Dollars	–	–
Sterling	–	3,467
Euro and other currencies	364	3,715
	364	7,182
Total investments	4,973,048	5,089,315

*See note 2.1 for further details.

18 Loans and receivables including insurance receivables

	2018 $000	2017 (restated)* $000
Gross receivables arising from insurance and reinsurance contracts	1,143,886	1,004,032
Provision for impairment	(2,132)	(2,219)
Net receivables arising from insurance and reinsurance contracts	1,141,754	1,001,813
Due from contract holders, brokers, agents and intermediaries	751,008	650,549
Due from reinsurance operations	390,746	351,264
	1,141,754	1,001,813
Prepayments and accrued income	26,127	15,263
Other loans and receivables:		
Net profit commission receivable	16,300	22,961
Accrued interest	20,947	18,332
Share of Syndicates' other debtors' balances	27,767	30,309
Other debtors including related party amounts	32,215	32,774
Total loans and receivables including insurance receivables	1,265,110	1,121,452

The amounts expected to be recovered before and after one year are estimated as follows:

	2018 $000	2017 (restated)* $000
Within one year	1,138,873	980,660
After one year	126,237	140,792
	1,265,110	1,121,452

*See note 2.1 for further details.

There is no significant concentration of credit risk with respect to loans and receivables as the Group has a large number of internationally dispersed debtors. The Group has recognised a gain of $87,000 (2017: loss of $474,000) for the impairment of receivables during the year ended 31 December 2018. This is recorded under operational expenses in the consolidated income statement. The carrying amounts disclosed above are reasonably approximate to the fair value at the reporting date.

19 Derivative financial instruments

The Group entered into both exchange-traded and over-the-counter derivative contracts for a number of purposes during 2018. The Group had the right and intention to settle each contract on a net basis. The assets and liabilities of these contracts at 31 December 2018 all mature within one year of the balance sheet date and are detailed below:

31 December 2018 Derivative financial instruments included on balance sheet	Gross contract notional amount $000	Fair value of assets $000	Fair value of liabilities $000	Net balance sheet position $000
Foreign exchange forward contracts	104,627	1,451	(599)	852
Interest rate futures contracts	118,497	–	(480)	(480)

The foreign exchange forward contracts are represented by gross fair value of assets and liabilities as detailed below:

Gross fair value of assets	72,568	32,913	105,481
Gross fair value of liabilities	(71,117)	(33,512)	(104,629)
	1,451	(599)	852

31 December 2017 (restated)* Derivative financial instruments included on balance sheet	Gross contract notional amount $000	Fair value of assets $000	Fair value of liabilities $000	Net balance sheet position $000
Foreign exchange forward contracts	40,765	186	(163)	23
Interest rate futures contracts	164,865	224	–	224

The foreign exchange forward contracts are represented by gross fair value of assets and liabilities as detailed below:

Gross fair value of assets	18,661	22,549	41,210
Gross fair value of liabilities	(18,475)	(22,712)	(41,187)
	186	(163)	23

*See note 2.1 for further details.

Foreign exchange forward contracts

During the current and prior year the Group entered into a series of conventional over-the-counter forward contracts in order to secure translation gains made on Euro, US Dollar and other non-Pound Sterling denominated monetary assets. The contracts require the Group to forward sell a fixed amount of the relevant currency for Pound Sterling at pre-agreed future exchange rates. The Group made a gain on these forward contracts of $1,539,000 (2017: loss of $964,000) as included in the investment result in note 7. There was no initial purchase cost associated with these instruments.

Interest rate futures contracts

During the year the Group continued short selling a number of government bond futures denominated in a range of currencies to informally hedge interest rate risk on specific long portfolios. All contracts are exchange traded and the Group made a loss on these futures contracts of $259,000 (2017: loss of $545,000) as included in the investment result in note 7.

Equity index options

During the year, no equity index futures were purchased. All contracts held in prior years were exchange traded in 2017 and the Group made a loss on these future contracts of $186,000 as included in the investment result in note 7.

20 Fair value measurements

In accordance with IFRS 13 *Fair Value Measurement,* the fair value of financial instruments based on a three-level fair value hierarchy that reflects the significance of the inputs used in measuring the fair value, is set out below.

As at 31 December 2018	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
Financial assets				
Debt and fixed income securities	1,509,012	3,065,617	–	4,574,629
Equities and shares in unit trusts	–	379,139	18,916	398,055
Deposits with credit institutions	364	–	–	364
Insurance-linked funds	–	–	55,182	55,182
Derivative financial instruments	–	1,451	–	1,451
Total	1,509,376	3,446,207	74,098	5,029,681
Financial liabilities				
Derivative financial instruments	–	1,079	–	1,079
Total	–	1,079	–	1,079

As at 31 December 2017	Level 1 $000	Level 2 $000	Level 3 $000	Total (restated)* $000
Financial assets				
Debt and fixed income securities	1,610,461	3,020,367	–	4,630,828
Equities and shares in unit trusts	–	435,934	15,371	451,305
Deposits with credit institutions	7,182	–	–	7,182
Insurance-linked funds	–	–	49,918	49,918
Derivative financial instruments	–	410	–	410
Total	1,617,643	3,456,711	65,289	5,139,643
Financial liabilities				
Derivative financial instruments	–	163	–	163
Total	–	163	–	163

*See note 2.1 for further details.

The levels of the fair value hierarchy are defined by the standard as follows:
- Level 1 – fair values measured using quoted prices (unadjusted) in active markets for identical instruments;
- Level 2 – fair values measured using directly or indirectly observable inputs or other similar valuation techniques for which all significant inputs are based on market observable data;
- Level 3 – fair values measured using valuation techniques for which significant inputs are not based on market observable data.

The fair values of the Group's financial assets are based on prices provided by investment managers who obtain market data from numerous independent pricing services. The pricing services used by the investment manager obtain actual transaction prices for securities that have quoted prices in active markets. For those securities which are not actively traded, the pricing services use common market valuation pricing models. Observable inputs used in common market valuation pricing models include, but are not limited to, broker quotes, credit ratings, interest rates and yield curves, prepayment speeds, default rates and other such inputs which are available from market sources.

Investments in mutual funds, which are included in equities and shares in unit trusts, comprise a portfolio of stock investments in trading entities which are invested in various quoted investments. The fair value of shares in unit trusts is based on the net asset value of the fund as reported by independent pricing sources or the fund manager.

Included within Level 1 of the fair value hierarchy are certain government bonds, treasury bills, long-term debt and exchange-traded equities which are measured based on quoted prices in active markets. The fair value of the long-term debt that is carried at amortised cost, is estimated at $706.3 million (2017: $428.5 million) and is considered as Level 1 in the fair value hierarchy.

Level 2 of the hierarchy contains certain government bonds, US government agencies, corporate securities, asset backed securities and mortgage-backed securities. The fair value of these assets is based on the prices obtained from both investment managers and investment custodians as discussed above. The Group records the unadjusted price provided and validates the price through a number of methods including a comparison of the prices provided by the investment managers with the investment custodians and the valuation used by external parties to derive fair value. Quoted prices for US government agencies and corporate securities are based on a limited number of transactions for those securities and as such the Group considers these instruments to have similar characteristics to those instruments classified as Level 2. Also included within Level 2 are units held in traditional long funds and long and short special funds and over-the-counter derivatives.

20 Fair value measurements continued

Level 3 contains investments in a limited partnership, unquoted equity securities and insurance-linked funds which have limited observable inputs on which to measure fair value. Unquoted equities, including equity instruments in limited partnerships are carried at fair value. Fair value is determined to be net asset value for the limited partnerships, and for the equity holdings it is determined to be the latest available traded price. The effect of changing one or more inputs used in the measurement of fair value of these instruments to another reasonably possible assumption would not be significant. At 31 December 2018, the insurance-linked fund of $55,182,000 represents the Group's investment in the Kiskadee Funds (2017: $49,918,000).

The fair value of the Kiskadee Funds is estimated to be the net asset value as at the balance sheet date. The net asset value is based on the fair value of the assets and liabilities in the Fund. The majority of the assets of the Funds are cash and cash equivalents. Significant inputs and assumptions in calculating the fair value of the assets and liabilities associated with reinsurance contracts written by the Kiskadee Funds include the amount and timing of claims payable in respect of claims incurred and periods of unexpired risk. The Group has considered changes in the net asset valuation of the Kiskadee Funds if reasonably different inputs and assumptions were used and has found no significant changes in the valuation.

In certain cases, the inputs used to measure the fair value of a financial instrument may fall into more than one level within the fair value hierarchy. In this instance, the fair value of the instrument in its entirety is classified based on the lowest level of input that is significant to the fair value measurement.

The Group's policy is to recognise transfers into and transfers out of fair value hierarchy levels at the end of the relevant reporting period during which the transfers are deemed to have occurred.

During the year, there were no transfers made between Level 1, Level 2 or Level 3 of the fair value hierarchy.

The following table sets forth a reconciliation of opening and closing balances for financial instruments classified under Level 3 of the fair value hierarchy:

31 December 2018	Financial assets		
	Equities and shares in unit trusts $000	Insurance linked fund $000	Total $000
Balance at 1 January	15,371	49,918	65,289
Fair value gains or losses through profit or loss*	(381)	(3,140)	(3,521)
Foreign exchange losses	(708)	–	(708)
Purchases	5,000	9,339	14,339
Settlements	(366)	(935)	(1,301)
Closing balance	**18,916**	**55,182**	**74,098**
Unrealised gains and losses in the year on securities held at the end of the year	**(381)**	**(3,140)**	**(3,521)**

*Fair value gains/(losses) are included within the investment result in the income statement for equities and shares in unit trusts and through other income for the insurance-linked fund.

31 December 2017 (restated)†	Financial assets		
	Equities and shares in unit trusts $000	Insurance linked fund $000	Total $000
Balance at 1 January	15,072	58,058	73,130
Fair value gains or losses through profit or loss*	(440)	(7,360)	(7,800)
Foreign exchange gains/(losses)	1,010	(203)	807
Purchases	753	5,156	5,909
Settlements	(1,024)	(5,733)	(6,757)
Closing balance	15,371	49,918	65,289
Unrealised gains and losses in the year on securities held at the end of the year	(329)	(9,129)	(9,458)

*Fair value gains/(losses) are included within the investment result in the income statement for equities and shares in unit trusts and through other income for the insurance-linked fund.
†See note 2.1 for further details.

21 Cash and cash equivalents

	2018 $000	2017 (restated)* $000
Cash at bank and in hand	1,124,346	708,753
Short-term deposits	164,505	159,014
Total	1,288,851	867,767

*See note 2.1 for further details.

The Group holds its cash deposits with a well-diversified range of banks and financial institutions. Cash includes overnight deposits. Short-term deposits include debt securities with an original maturity date of less than three months and money market funds.

22 Share capital

	31 December 2018		31 December 2017 (restated)*	
Group	Share capital $000	Number of shares 000	Share capital $000	Number of shares 000
Authorised ordinary share capital of 6.5p (2017: 6.5p)	425,760	3,692,308	425,760	3,692,308
Issued ordinary share capital of 6.5p (2017: 6.5p)	33,986	295,315	33,913	294,484

*See note 2.1 for further details.

The amounts presented in the equity structure of the Group above relate to Hiscox Ltd, the legal Parent Company.

Changes in Group share capital and contributed surplus	Ordinary share capital $000	Share premium $000	Contributed surplus $000
At 1 January 2017 (restated)*	33,806	34,031	183,969
Employee share option scheme – proceeds from shares issued	77	6,084	–
Scrip dividends to owners of the Company	30	5,734	–
At 31 December 2017 (restated)*	33,913	45,849	183,969
Employee share option scheme – proceeds from shares issued	41	4,013	–
Scrip dividends to owners of the Company	32	7,818	–
At 31 December 2018	33,986	57,680	183,969

*See note 2.1 for further details.

Contributed surplus is a distributable reserve and arose on the reverse acquisition of Hiscox plc on 12 December 2006.

During the year, the Group offered its shareholders the option of receiving a scrip dividend alternative to the interim cash dividend. This resulted in the Company paying the shareholders, who opted for a scrip dividend, in shares of equal value to the cash dividend at a specified date. The full dividend was distributed from retained earnings, and the new shares issued for the scrip dividend were reflected in share capital and share premium.

The Company relies upon dividend streams from its subsidiary companies to provide the cash flow required for distributions to be made to shareholders. The ability of the subsidiaries to pay dividends is subject to regulatory restrictions within the jurisdiction from which they operate.

Share repurchase

The Trustees of the Group's Employee Benefit Trust purchased $76,474,000 of shares (2017: $nil) to facilitate the settlement of vesting awards under the Group's Performance Share Plan. As the trust is consolidated into the Group financial results, these purchases have been accounted for in the same way as treasury shares and have been charged against retained earnings. The shares are held by the trustees for the beneficiaries of the Trust.

Equity structure of Hiscox Ltd	Note	Number of ordinary shares in issue (thousands) 2018	Number of ordinary shares in issue (thousands) 2017
At 1 January		294,484	293,227
Employee share option scheme – ordinary shares issued		460	897
Scrip dividends to owners of the Company	29	371	360
At 31 December		295,315	294,484

All issued shares are fully paid.

22 Share capital continued

Share options and Performance Share Plan awards

Performance Share Plan awards are granted to Directors and to senior employees. No exercise price is attached to performance plan awards, although their attainment is conditional on the employee completing three years' service (the vesting period) and the Group achieving targeted levels of returns on equity. Share options are also conditional on the employees completing three years' service (the vesting period) or less under exceptional circumstances (death, disability, retirement or redundancy). The options are exercisable starting three years from the grant date only if the Group achieves its targets of return on equity; the options have a contractual option term of ten years. The Group has no legal or constructive obligation to repurchase or settle the options in cash.

In accordance with IFRS 2 the Group recognises an expense for the fair value of share option and Performance Share Plan award instruments issued to employees, over their vesting period through the income statement. The amount recognised in the consolidated income statement during the year was income of $3,638,000 (2017: expense of $32,465,000). This comprises income of $4,641,000 (2017: expense of $31,439,000) in respect of Performance Share Plan awards and an expense of $1,002,000 (2017: expense of $1,026,000) in respect of share option awards. The Group has applied the principles outlined in the Black-Scholes option pricing model when determining the fair value of each share option instrument.

The range of principal Group assumptions applied in determining the fair value of share-based payment instruments granted during the year under review are:

Assumptions affecting inputs to fair value models	2018	2017
Annual risk-free rates of return and discount rates (%)	**0.83-0.89**	0.19-0.26
Long-term dividend yield (%)	**3.05**	3.09
Expected life of options (years)	**3.25**	3.25
Implied volatility of share price (%)	**22.0**	22.0
Weighted average share price (p)	**1,497.8**	1,139.3

The weighted average fair value of each share option granted during the year was 302.5p (2017: 223.6p). The weighted average fair value of each Performance Share Plan award granted during the year was 1,492.9p (2017: 1,127.1p).

Movements in the number of share options and Performance Share Plan awards during the year and details of the balances outstanding at 31 December 2018 for the Executive Directors are shown in the annual report on remuneration 2018. The total number of options and Performance Share Plan awards outstanding is 9,804,430 (2017: 10,009,723) of which 3,032,437 are exercisable (2017: 2,966,870). The total number of SAYE options outstanding is 1,528,496 (2017: 1,580,570).

The implied volatility assumption is based on historical data for periods of between five and ten years immediately preceding grant date.

For options issued after 1 January 2006 the assumptions regarding long-term dividend yield have been aligned to the progressive dividend policy announced during the 2005 Rights Issue.

23 Insurance liabilities and reinsurance assets

	Note	2018 $000	2017 (restated)* $000
Gross			
Claims reported and claim adjustment expenses		1,957,222	1,626,087
Claims incurred but not reported		3,034,981	2,724,479
Unearned premiums		1,709,272	1,657,184
Total insurance liabilities, gross		6,701,475	6,007,750
Recoverable from reinsurers			
Claims reported and claim adjustment expenses		690,569	488,237
Claims incurred but not reported		1,356,530	1,004,061
Unearned premiums		409,476	340,957
Total reinsurers' share of insurance liabilities	16	2,456,575	1,833,255
Net			
Claims reported and claim adjustment expenses		1,266,653	1,137,850
Claims incurred but not reported		1,678,451	1,720,418
Unearned premiums		1,299,796	1,316,227
Total insurance liabilities, net		4,244,900	4,174,495

The net amounts expected to be recovered and settled before and after one year, based on historical experience, are estimated as follows:

	2018 $000	2017 (restated)* $000
Within one year	2,422,679	2,400,924
After one year	1,822,221	1,773,571
	4,244,900	4,174,495

*See note 2.1 for further details.

The gross claims reported, the claims adjustment expenses liabilities and the liability for claims incurred but not reported are net of expected recoveries from salvage and subrogation. The amounts for salvage and subrogation at the end of 2018 and 2017 are not material.

23 Insurance liabilities and reinsurance assets continued

23.1 Insurance contracts assumptions

(a) Process used to decide on assumptions

There are many risks associated with insurance contracts, and this means that there is a considerable amount of uncertainty in estimating the future settlement cost of claims. There is uncertainty in both the amounts and the timing of future claim payment cash flows.

Claims paid are claims transactions settled up to the reporting date including settlement expenses allocated to those transactions.

Unpaid claims reserves are made for known or anticipated liabilities which have not been settled up to the reporting date. Included within the provision is an allowance for the future costs of settling those claims.

The Group relies on actuarial analysis to estimate the settlement cost of future claims. There is close communication between the actuaries and other key stakeholders, such as the underwriters, claims and finance teams when setting and validating the assumptions. The unpaid claims reserve is estimated based on past experience and current expectations of future cost levels. Allowance is made for the current premium rating and inflationary environment.

The claim reserves are estimated on a best estimate basis, taking into account current market conditions and the nature of risks being underwritten.

Under certain insurance contracts, the Group may be permitted to sell property acquired in settling a claim (for example, salvage). The Group may also have the right to pursue third parties for payment of some or all costs (for example, subrogation). If it is certain a recovery or reimbursement will be made at the valuation date, specific estimates of these salvage and/or subrogation amounts are included as allowances in the measurement of the insurance liability for unpaid claims. This is then recognised in insurance and reinsurance receivables when the liability is settled.

Estimates of where claim liabilities will ultimately settle are adjusted each reporting period to reflect emerging claims experience. Changes in expected claims may result in a reduction or an increase in the ultimate claim costs and a release or an increase in reserves in the period in which the change occurs.

Booked reserves are held above the best estimate to help mitigate the uncertainty within the reserve estimates. As the best estimate matures and becomes more certain, the management margin is gradually released in line with the reserving policy. This approach is consistent with last year.

(b) Claims development tables

The development of insurance liabilities provides a measure of the Group's ability to estimate the ultimate value of claims. The Group analyses actual claims development compared with previous estimates on an accident year basis. This exercise is performed to include the liabilities of Syndicate 33 at the 100% level regardless of the Group's actual level of ownership. Analysis at the 100% level is required in order to avoid distortions arising from reinsurance to close arrangements which subsequently increase the Group's share of ultimate claims for each accident year, three years after the end of that accident year.

The top half of each table, on the following pages, illustrates how estimates of ultimate claim costs for each accident year have changed at successive year ends. The bottom half reconciles cumulative claim costs to the amounts still recognised as liabilities. A reconciliation of the liability at the 100% level to the Group's share, as included in the Group balance sheet, is also shown.

23 Insurance liabilities and reinsurance assets

23.1 Insurance contracts assumptions

(b) Claims development tables continued

Insurance claims and claim adjustment expenses reserves – gross at 100%

Accident year	2009 $000	2010 $000	2011 $000	2012 $000	2013 $000	2014 $000	2015 $000	2016 $000	2017 $000	**2018 $000**	**Total $000**
Estimate of ultimate claims costs as adjusted for foreign exchange* at end of accident year:	1,257,195	1,522,742	1,951,781	1,623,266	1,307,839	1,432,809	1,539,243	1,913,464	3,370,767	**3,129,834**	**19,048,940**
one year later	1,029,375	1,281,949	1,753,802	1,441,377	1,143,133	1,215,388	1,375,233	1,699,442	3,058,051	**–**	**13,997,750**
two years later	943,522	1,193,676	1,700,298	1,331,898	1,016,916	1,127,259	1,267,856	1,609,341	–	**–**	**10,190,766**
three years later	938,199	1,174,939	1,715,202	1,327,293	949,298	1,081,118	1,263,033	–	–	**–**	**8,449,082**
four years later	937,351	1,143,832	1,688,798	1,316,119	948,159	1,056,275	–	–	–	**–**	**7,090,534**
five years later	931,294	1,125,507	1,639,391	1,306,145	925,591	–	–	–	–	**–**	**5,927,928**
six years later	913,063	1,097,412	1,571,359	1,312,011	–	–	–	–	–	**–**	**4,893,845**
seven years later	910,334	1,080,226	1,533,346	–	–	–	–	–	–	**–**	**3,523,906**
eight years later	888,036	1,082,618	–	–	–	–	–	–	–	**–**	**1,970,654**
nine years later	894,574	–	–	–	–	–	–	–	–	**–**	**894,574**
Current estimate of cumulative claims	894,574	1,082,618	1,533,346	1,312,011	925,591	1,056,275	1,263,033	1,609,341	3,058,051	**3,129,834**	**15,864,674**
Cumulative payments to date	(842,797)	(1,004,617)	(1,471,251)	(1,130,716)	(844,354)	(894,830)	(932,960)	(1,115,170)	(1,485,290)	**(538,004)**	**(10,259,989)**
Liability recognised at 100% level	51,777	78,001	62,095	181,295	81,237	161,445	330,073	494,171	1,572,761	**2,591,830**	**5,604,685**
Liability recognised in respect of prior accident years at 100% level											**135,491**
Total gross liability to external parties at 100% level											**5,740,176**

*The foreign exchange adjustment arises from the retranslation of the estimates at each date using the exchange rate ruling at 31 December 2018.

Reconciliation of 100% disclosures above to Group's share – gross

Accident year	2009 $000	2010 $000	2011 $000	2012 $000	2013 $000	2014 $000	2015 $000	2016 $000	2017 $000	**2018 $000**	**Total $000**
Current estimate of cumulative claims	894,574	1,082,618	1,533,346	1,312,011	925,591	1,056,275	1,263,033	1,609,341	3,058,051	**3,129,834**	**15,864,674**
Less: attributable to external Names	(152,292)	(172,037)	(222,595)	(170,889)	(100,990)	(114,988)	(133,332)	(176,949)	(415,375)	**(393,572)**	**(2,053,019)**
Group's share of current ultimate claims estimate	742,282	910,581	1,310,751	1,141,122	824,601	941,287	1,129,701	1,432,392	2,642,676	**2,736,262**	**13,811,655**
Cumulative payments to date	(842,797)	(1,004,617)	(1,471,251)	(1,130,716)	(844,354)	(894,830)	(932,960)	(1,115,170)	(1,485,290)	**(538,004)**	**(10,259,989)**
Less: attributable to external Names	147,319	154,918	211,456	149,961	89,715	96,600	96,597	124,138	199,542	**62,894**	**1,333,140**
Group's share of cumulative payments	(695,478)	(849,699)	(1,259,795)	(980,755)	(754,639)	(798,230)	(836,363)	(991,032)	(1,285,748)	**(475,110)**	**(8,926,849)**
Liability for 2009 to 2017 accident years recognised on Group's balance sheet	46,804	60,882	50,956	160,367	69,962	143,057	293,338	441,360	1,356,928	**2,261,152**	**4,884,806**
Liability for accident years before 2009 recognised on Group's balance sheet											**107,397**
Total Group liability to external parties included in balance sheet – gross**											**4,992,203**

**This represents the claims element of the Group's insurance liabilities.

23 Insurance liabilities and reinsurance assets

23.1 Insurance contracts assumptions

(b) Claims development tables continued

Insurance claims and claim adjustment expenses reserves – net of reinsurance at 100%

Accident year	2009 $000	2010 $000	2011 $000	2012 $000	2013 $000	2014 $000	2015 $000	2016 $000	2017 $000	**2018 $000**	Total $000
Estimate of ultimate claims costs as adjusted for foreign exchange* at end of accident year:	1,043,379	1,188,318	1,478,605	1,165,479	1,112,603	1,160,605	1,235,375	1,449,168	1,834,262	**1,788,472**	13,456,266
one year later	825,472	1,062,739	1,352,903	1,029,861	987,409	1,019,248	1,142,638	1,314,857	1,612,635	**–**	10,347,762
two years later	801,024	990,215	1,307,656	953,721	886,480	926,170	1,049,091	1,241,805	–	**–**	8,156,162
three years later	806,113	959,124	1,309,295	918,129	822,113	871,962	1,042,224	–	–	**–**	6,728,960
four years later	790,438	932,291	1,300,256	908,905	817,967	842,898	–	–	–	**–**	5,592,755
five years later	788,586	926,775	1,248,025	929,198	792,666	–	–	–	–	**–**	4,685,250
six years later	771,822	895,406	1,211,680	919,205	–	–	–	–	–	**–**	3,798,113
seven years later	766,346	880,933	1,178,552	–	–	–	–	–	–	**–**	2,825,831
eight years later	745,754	874,749	–	–	–	–	–	–	–	**–**	1,620,503
nine years later	744,878	–	–	–	–	–	–	–	–	**–**	744,878
Current estimate of cumulative claims	744,878	874,749	1,178,552	919,205	792,666	842,898	1,042,224	1,241,805	1,612,635	**1,788,472**	11,038,084
Cumulative payments to date	(705,061)	(826,955)	(1,131,680)	(782,619)	(724,120)	(684,741)	(743,175)	(853,452)	(948,085)	**(423,922)**	(7,823,810)
Liability recognised at 100% level	39,817	47,794	46,872	136,586	68,546	158,157	299,049	388,353	664,550	**1,364,550**	3,214,274
Liability recognised in respect of prior accident years at 100% level											91,079
Total net liability to external parties at 100% level											3,305,353

*The foreign exchange adjustment arises from the retranslation of the estimates at each date using the exchange rate ruling at 31 December 2017.

Reconciliation of 100% disclosures above to Group's share – net of reinsurance

Accident year	2009 $000	2010 $000	2011 $000	2012 $000	2013 $000	2014 $000	2015 $000	2016 $000	2017 $000	**2018 $000**	Total $000
Current estimate of cumulative claims	744,878	874,749	1,178,552	919,205	792,666	842,898	1,042,224	1,241,805	1,612,635	**1,788,472**	11,038,084
Less: attributable to external Names	(124,850)	(131,534)	(166,805)	(104,417)	(85,490)	(89,395)	(108,754)	(129,538)	(176,805)	**(182,260)**	(1,299,848)
Group's share of current ultimate claims estimate	620,028	743,215	1,011,747	814,788	707,176	753,503	933,470	1,112,267	1,435,830	**1,606,212**	9,738,236
Cumulative payments to date	(705,061)	(826,955)	(1,131,680)	(782,619)	(724,120)	(684,741)	(743,175)	(853,452)	(948,085)	**(423,922)**	(7,823,810)
Less: attributable to external Names	120,237	121,142	157,600	87,455	75,164	73,447	75,132	90,132	115,294	**44,945**	960,548
Group's share of cumulative payments	(584,824)	(705,813)	(974,080)	(695,164)	(648,956)	(611,294)	(668,043)	(763,320)	(832,791)	**(378,977)**	(6,863,262)
Liability for 2009 to 2018 accident years recognised on Group's balance sheet	35,204	37,402	37,667	119,624	58,220	142,209	265,427	348,947	603,039	**1,227,235**	2,874,974
Liability for accident years before 2009 recognised on Group's balance sheet											70,130
Total Group liability to external parties included in balance sheet – net**											2,945,104

**This represents the claims element of the Group's insurance liabilities and reinsurance assets.

23 Insurance liabilities and reinsurance assets continued

23.2 Movements in insurance claims liabilities and reinsurance claims assets

A reconciliation of the insurance claims liabilities is as follows:

Year ended 31 December	2018 Gross $000	2018 Reinsurance $000	2018 Net $000	2017 (restated)* Gross $000	2017 (restated)* Reinsurance $000	2017 (restated)* Net $000
Total at beginning of year	**4,350,566**	**(1,492,298)**	**2,858,268**	3,181,622	(673,463)	2,508,159
Claims and claim adjustment expenses for year	**2,326,632**	**(1,100,803)**	**1,225,829**	2,489,598	(1,178,682)	1,310,916
Cash paid for claims settled in the year	**(1,567,242)**	**531,815**	**(1,035,427)**	(1,427,543)	370,484	(1,057,059)
Foreign exchange and other adjustments	**(117,753)**	**14,187**	**(103,566)**	106,889	(10,637)	96,252
Total at end of year	**4,992,203**	**(2,047,099)**	**2,945,104**	4,350,566	(1,492,298)	2,858,268
Claims reported and claim adjustment expenses	**1,957,222**	**(690,569)**	1,266,653	1,626,087	(488,237)	1,137,850
Claims incurred but not reported	**3,034,981**	**(1,356,530)**	1,678,451	2,724,479	(1,004,061)	1,720,418
Total at end of year	**4,992,203**	**(2,047,099)**	**2,945,104**	4,350,566	(1,492,298)	2,858,268

The insurance claims expense reported in the consolidated income statement is comprised as follows:

Year ended 31 December	2018 Gross $000	2018 Reinsurance $000	2018 Net $000	2017 (restated)* Gross $000	2017 (restated)* Reinsurance $000	2017 (restated)* Net $000
Current year claims and claim adjustment expenses	**2,780,093**	**(1,227,812)**	**1,552,281**	2,911,356	(1,265,918)	1,645,438
Over-provision in respect of prior year claims and claim adjustment expenses	**(453,461)**	**127,009**	**(326,452)**	(421,758)	97,548	(324,210)
Acquisitions/(divestments) and transfers†	**–**	**–**	**–**	–	(10,312)	(10,312)
Total claims and claim adjustment expenses	**2,326,632**	**(1,100,803)**	**1,225,829**	2,489,598	(1,178,682)	1,310,916

†The net movement in 2018 and 2017 relates to a retroactive reinsurance arrangement that transferred the benefits and risks of some of the Group's insurance portfolio.

A reconciliation of the unearned premium reserves is as follows:

	2018 Gross $000	2018 Reinsurance $000	2018 Net $000	2017 (restated)* Gross $000	2017 (restated)* Reinsurance $000	2017 (restated)* Net $000
Balance deferred at 1 January	**1,657,184**	**(340,957)**	**1,316,227**	1,596,071	(325,542)	1,270,529
Premiums written	**3,778,341**	**(1,196,855)**	**2,581,486**	3,286,021	(883,022)	2,402,999
Premiums earned through the income statement	**(3,699,802)**	**1,126,163**	**(2,573,639)**	(3,295,965)	879,757	(2,416,208)
Foreign exchange and other adjustments	**(26,451)**	**2,173**	**(24,278)**	71,057	(12,150)	58,907
Balance deferred at 31 December	**1,709,272**	**(409,476)**	**1,299,796**	1,657,184	(340,957)	1,316,227

*See note 2.1 for further details.

The amounts expected to be recovered before and after one year, based on historical experience, are included in the first table to this note 23.

24 Trade and other payables

	Note	2018 $000	2017 (restated)* $000
Creditors arising out of direct insurance operations		**74,079**	82,257
Creditors arising out of reinsurance operations		**664,803**	504,423
		738,882	586,680
Share of Syndicates' other creditors' balances		**5,770**	8,597
Social security and other taxes payable		**31,066**	27,122
Other creditors		**21,999**	14,334
		58,835	50,053
Reinsurers' share of deferred acquisition costs	15	**106,758**	91,805
Accruals and deferred income		**176,605**	160,464
Total		**1,081,080**	889,002

*See note 2.1 for further details.

Included within accruals and deferred income is $7.0 million (2017: $10.9 million) of deferred gain on retroactive reinsurance contracts.

24 Trade and other payables continued

The amounts expected to be settled before and after one year are estimated as follows:

	2018 $000	2017 (restated)* $000
Within one year	947,580	743,202
After one year	133,500	145,800
	1,081,080	889,002

*See note 2.1 for further details.

The amounts expected to be settled after one year of the balance sheet date primarily relate to reinsurance creditors.

The carrying amounts disclosed above are reasonably approximate to the fair value at the reporting date.

25 Tax expense

The Company and its subsidiaries are subject to enacted tax laws in the jurisdictions in which they are incorporated and domiciled. The principal subsidiaries of the Company and the country in which they are incorporated are listed in note 32. The amounts charged in the consolidated income statement comprise the following:

	2018 $000	2017 (restated)* $000
Current tax		
Expense for the year	19,659	24,483
Adjustments in respect of prior years	1,529	(106)
Total current tax expense	21,188	24,377
Deferred tax		
Credit for the year	(11,292)	(27,353)
Adjustments in respect of prior years	(1,017)	7,335
Effect of rate change	497	1,429
Total deferred tax credit	(11,812)	(18,589)
Total tax charged to the income statement	9,376	5,788

The standard rate of corporation tax in Bermuda is 0% whereas the effective rate of tax for the Group is 6.82% (2017: 14.6%).

A reconciliation of the difference is provided below:

	2018 $000	2017 (restated)* $000
Profit before tax	137,375	39,692
Tax calculated at the standard corporation tax rate applicable in Bermuda: 0% (2017: 0%)	–	–
Effects of Group entities subject to overseas tax at different rates	4,411	(4,391)
Impact of overseas tax rates on:		
Effect of rate change	497	1,429
Expenses not deductible for tax purposes	1,425	2,159
Tax losses for which no deferred tax asset is recognised	5,303	6,673
Other	1,273	430
Adjustment for share-based payments	(216)	(758)
Non-taxable income	(3,829)	(6,984)
Prior year tax adjustments	512	7,230
Tax charge for the period	9,376	5,788

*See note 2.1 for further details.

The UK Finance Act 2015 introduced a new tax with effect from April 2015, the Diverted Profits Tax (DPT), which in certain situations applies a tax of 25% to income which would not otherwise be chargeable to UK tax. The Group has been proactively engaged in ongoing discussions with the UK's tax authority regarding taxing rights in respect to one long-standing intra-group arrangement. If this transaction is found to be subject to DPT, it would result in a material adverse effect on the Group results. We consider the probability of this outcome to be low, and accordingly no provision is made for DPT in the Group's accounts at 31 December 2018. As the discussion with the UK's tax authority is ongoing, the Group expects disclosure of the potential exposure to prejudice seriously its position with the other party in the matter.

26 Deferred tax

Net deferred tax assets	2018 $000	2017 (restated)* $000
Trading losses in overseas entities	47,540	46,601
Deferred tax assets	48,036	20,442
Deferred tax liabilities	(34,903)	(13,581)
Total deferred tax asset	60,673	53,462

Net deferred tax liabilities	2018 $000	2017 $000
Deferred tax assets	–	–
Deferred tax liabilities	–	–
Total net deferred tax liability	–	–

Deferred tax assets and deferred tax liabilities relating to the same tax authority are presented net in the Group's balance sheet.

Net Group deferred tax assets/(liabilities) analysed by balance sheet headings

At 31 December	2017 (restated)* $000	Income statement (charge)/credit $000	Recognised in other comprehensive income/equity $000	Foreign exchange $000	2018 $000
Tangible assets	327	(83)	–	(13)	231
UK capital losses	–	800	–	(36)	764
Trade and other payables	3,401	(300)	–	(177)	2,924
Intangible assets – Syndicate capacity	1,878	(196)	–	(100)	1,582
Retirement benefit obligations	11,202	12	(4,135)	(450)	6,629
Open years of account	13,626	12,406	–	(1,325)	24,707
Other items	14,759	(3,093)	237	(704)	11,199
Total deferred tax assets	45,193	9,546	(3,898)	(2,805)	48,036
Financial assets	(1,118)	(535)	–	87	(1,566)
Insurance contracts – equalisation provision	(26,089)	6,752	–	1,173	(18,164)
Reinsurance premiums	(11,125)	(4,894)	–	846	(15,173)
Total deferred tax liabilities	(38,332)	1,323	–	2,106	(34,903)
Net total deferred tax assets/(liabilities)	6,861	10,869	(3,898)	(699)	13,133
Trading losses in overseas entities	46,601	948	–	(9)	47,540
Net total deferred tax assets/(liabilities)	6,861	10,869	(3,898)	(699)	13,133
Net deferred tax position asset/(liability)	53,462	11,817	(3,898)	(708)	60,673

*See note 2.1 for further details.

Following changes to the future UK main rate of corporation tax introduced in the Finance Act 2016, the deferred tax on the Syndicates' open years of account is calculated with reference to the tax rate expected to be in force when those years close. Equally, the deferred tax liability on equalisation provision is calculated at the tax rate expected to be applicable as it unwinds. All other UK deferred income tax assets and liabilities are calculated at 17% for the year ended 31 December 2018 (2017: 17%).

Movements in deferred and current tax relating to tax deductions arising on employee share options are recognised in the statement of changes in equity to the extent that the movement exceeds the corresponding charge to the income statement. Movements in deferred tax relating to the employee retirement benefit obligation are recognised in the statement of comprehensive income to the extent that the movement corresponds to actuarial gains and losses recognised in the statement of comprehensive income. The total recognised outside the income statement is $151,000 income (2017: income of £4,553,000), comprising $3,897,000 deferred tax expense and $4,048,000 current tax income (2017: $1,053,000 deferred tax income and $3,500,000 current tax income).

26 Deferred tax

Net Group deferred tax assets/(liabilities) analysed by balance sheet headings ***continued***

Deferred tax assets of $47,540,000 (2017: $46,601,000), relating to losses arising in overseas entities, which depend on the availability of future taxable profits, have been recognised. Business projections indicate it is probable that sufficient future taxable income will be available against which to offset these recognised deferred tax assets within five years. $4,868,000 (2017: $1,682,000) of the tax losses to which these assets relate will expire within ten years; a further $42,672,000 (2017: $44,109,000) will expire after ten years. The Group has not provided for deferred tax assets totalling $13,946,000 (2017: $9,771,000) in relation to losses in overseas companies of $76,855,000 (2017: $53,611,000). In accordance with IAS 12, all deferred tax assets and liabilities are classified as non-current. The amount of deferred tax asset expected to be recovered after more than 12 months is $47,540,000 (2017: $45,791,000).

27 Employee retirement benefit obligations

The Company's subsidiary Hiscox plc operates a defined benefit pension scheme based on final pensionable salary. The scheme closed to future accrual with effect from 31 December 2006 and active members were offered membership of a defined contribution scheme from 1 January 2007. The funds of the defined benefit scheme are controlled by the trustee and are held separately from those of the Group. 61% of any scheme surplus or deficit is recharged to Syndicate 33. The full pension obligation of the Hiscox defined benefit pension scheme is recorded and the recovery from the third-party Names for their share of the Syndicate 33 recharge is shown as a separate asset.

The gross amount recognised in the Group balance sheet in respect of the defined benefit scheme is determined as follows:

	2018 $000	2017 (restated)* $000
Present value of scheme obligations	301,986	369,634
Fair value of scheme assets	(266,210)	(305,520)
Net amount recognised as a defined benefit obligation	**35,776**	64,114

As the present value of scheme obligations exceeds the fair value of the scheme assets, the scheme reports a deficit.

The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit actuarial cost method. A formal full actuarial valuation is performed on a triennial basis, most recently at 31 December 2017, and updated at each intervening balance sheet date by the actuaries. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of AA rated corporate bonds that have terms to maturity that approximate to the terms of the related pension liability.

The scheme assets are invested are as follows:

At 31 December	2018 $000	2017 (restated)* $000
Managed fund pooled investment vehicles		
UK equity funds	87,538	103,868
Emerging market equity funds	11,355	16,536
Global equity funds	46,271	52,180
Bond funds	72,958	81,632
US equities	28,464	30,252
Cash	19,624	21,052
	266,210	305,520

*See note 2.1 for further details.

27 Employee retirement benefit obligations continued

The amounts recognised in total comprehensive income are as follows:

	Note	2018 $000	2017 (restated)* $000
Past service cost		85	–
Interest cost on defined benefit obligation		9,292	9,291
Interest income on plan assets		(7,648)	(7,333)
Net interest cost		1,644	1,958
Administrative expenses and taxes		459	305
Total expense recognised in operational expenses in the income statement	9	2,188	2,263
Remeasurements			
Effect of changes in actuarial assumptions		(46,314)	4,816
Return on plan assets (excluding interest income)		21,990	(18,234)
Remeasurement of third-party Names share of defined benefit obligation		4,075	2,245
Total remeasurement included in other comprehensive income		(20,249)	(11,173)
Total defined benefit credit recognised in comprehensive income		(18,061)	(8,910)

In October 2018, the High Court in the UK issued a ruling to address inequalities in the calculation of guaranteed minimum pensions (GMPs) for members of pension schemes. This ruling requires pension funds to increase the benefits of some members of the pension scheme.

The Group has completed an estimate of the impact of the ruling on the scheme using one of the methods identified by the High Court (C2) for equalising GMPs. The Group has recognised a charge of £64,000 ($85,000) during the year.

The movement in liability recognised in the Group's balance sheet is as follows:

	2018 $000	2017 (restated)* $000
Group defined benefit liabilities at beginning of the year	64,114	69,612
Third-party Names' share of liability	(10,738)	(11,658)
Net defined benefit liability at beginning of year	53,376	57,954
Defined benefit cost included in net income	2,188	2,263
Contribution by employer	(3,733)	–
Credit from third-party Names	(367)	(379)
Foreign exchange movements	(2,028)	4,711
Total remeasurement included in other comprehensive income	(20,249)	(11,173)
Net defined benefit liability at end of year	29,187	53,376
Third-party Names' share of liability	6,589	10,738
Group defined benefit liability at end of year	35,776	64,114

A reconciliation of the fair value of scheme assets is as follows:

	2018 $000	2017 (restated)* $000
Opening fair value of scheme assets	305,520	266,517
Interest income	7,648	7,333
Cash flows		
Contribution by the employer	3,733	–
Benefit payments	(8,747)	(10,587)
Administration expenses	(459)	(305)
Remeasurements		
Return on plan assets (excluding interest income)	(21,990)	18,234
Foreign exchange movements	(19,495)	24,328
Closing fair value of scheme assets	266,210	305,520

*See note 2.1 for further details.

27 Employee retirement benefit obligations continued

A reconciliation of the present value of obligations of the scheme is as follows:

	2018 $000	2017 (restated)* $000
Opening present value of scheme obligations	369,634	336,129
Past service cost	85	–
Interest expense	9,292	9,291
Cash flows		
Benefit payments	(8,747)	(10,587)
Remeasurements		
Changes in actuarial assumptions	(46,314)	4,816
Foreign exchange movements	(21,964)	29,985
Closing present value of scheme obligations	301,986	369,634

*See note 2.1 for further details.

Assumptions regarding future mortality experience are set based on the S2PA light tables. Reductions in future mortality rates are allowed for by using the CMI 2017 projections (core model) with 1.25% p.a. long-term trend for improvements.

The average life expectancy in years of a pensioner retiring at age 60 on the balance sheet date is as follows:

	2018 years	2017 years
Male	27.9	28.6
Female	28.9	29.8

The average life expectancy in years of a pensioner retiring at 60, 15 years after the balance sheet date, is as follows:

	2018 years	2017 years
Male	28.9	29.9
Female	30.1	31.2

The weighted average duration of the defined benefit obligation at 31 December 2018 was 19.3 years (2017: 23.2 years).

Other principal actuarial assumptions are as follows:

	2018 %	2017 %
Discount rate	2.90	2.6
Inflation assumption (RPI)	3.10	3.1
Inflation assumption (CPI)	2.10	2.1
Pension increases	3.10	3.1

The scheme operates under UK trust law and the Trust is a separate legal entity from the Group. The scheme is governed by a board of trustees, comprised of member nominated and employer appointed trustees. The trustees are required by law to act in the best interests of scheme members and are responsible for setting certain policies together with the principal employer. The scheme is funded by the Group when required. Funding of the scheme is based on a separate actuarial valuation for funding purposes for which the assumptions may differ from the assumptions above. Funding requirements are formally set out in the statement of funding principles, schedule of contributions and recovery plan agreed between the trustees and the Group.

The triennial valuation carried out as at 31 December 2017 resulted in a deficit position of £26.5 million ($35.8 million) on a funding basis. The Group and the scheme's trustees have agreed a recovery plan to reduce the deficit and to eliminate the deficit by 2024. A funding contribution of £2.8 million ($3.7 million) was paid during 2018 and under the plan a further payment of £2.8 million ($3.6 million) will be made during 2019 and annually thereafter. The funding plan will be reviewed again following the next triennial funding valuation which will have an effective date of 31 December 2020.

While management believes that the actuarial assumptions are appropriate, any significant changes to those could affect the balance sheet and income statement. For example, an additional one year of life expectancy for all scheme members would increase the scheme obligations by £8,764,000 ($11,163,000) at 31 December 2018 (2017: £9,420,000 ($12,717,000)), and would increase the recorded net deficit on the balance sheet by the same amounts.

27 Employee retirement benefit obligations continued

The most sensitive and judgemental financial assumptions are the discount rate and inflation. These are considered further below. CPI revaluation in deferment is used for contracted-out members. Contracted-in members are linked to RPI as well as for all pension in payment increase.

The Group has estimated the sensitivity of the net obligation recognised in the consolidated balance sheet to isolated changes in these assumptions at 31 December 2018 as follows:

	Present value of unfunded obligations before change in assumption $000	Present value of unfunded obligations after change $000	(Increase) /decrease in obligation recognised on balance sheet $000
Effect of a change in discount rate			
Use of discount rate of 3.15%	35,776	21,834	13,942
Use of discount rate of 2.65%	35,776	50,723	(14,947)
Effect of a change in inflation			
Use of RPI inflation assumption of 3.35%	35,776	40,913	(5,137)
Use of RPI inflation assumption of 2.85%	35,776	30,967	4,809

28 Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares held by the Group and held in treasury as own shares.

Basic	2018	2017 (restated)*
Profit for the year attributable to the owners of the Company ($000)	127,999	33,904
Weighted average number of ordinary shares (thousands)	283,564	281,964
Basic earnings per share (cents per share)	45.1¢	12.0¢
Basic earnings per share (pence per share)	33.9p	9.3p

*See note 2.1 for further details.

Diluted

Diluted earnings per share is calculated adjusting for the assumed conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares, share options and awards. For the share options, a calculation is made to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	2018	2017 (restated)*
Profit for the year attributable to the owners of the Company ($000)	127,999	33,904
Weighted average number of ordinary shares in issue (thousands)	283,564	281,964
Adjustments for share options (thousands)	5,650	9,065
Weighted average number of ordinary shares for diluted earnings per share (thousands)	289,214	291,029
Diluted earnings per share (cents per share)	44.3¢	11.6¢
Diluted earnings per share (pence per share)	33.2p	9.0p

*See note 2.1 for further details.

Diluted earnings per share has been calculated after taking account of 5,103,924 (2017: 8,292,818) Performance Share Plan awards and 546,186 (2017: 772,427) options under SAYE schemes.

29 Dividends paid to owners of the Company

	2018 $000	2017 (restated)* $000
Final dividend for the year ended:		
31 December 2017 of 19.5p or 27.2¢ (net) per share	76,009	–
31 December 2016 of 19.0p or 23.6¢ (net) per share	–	67,664
Interim dividend for the year ended:		
31 December 2018 of 13.25¢ (net) per share	37,539	–
31 December 2017 of 9.5p or 12.6¢ (net) per share	–	36,044
	113,548	103,708

*See note 2.1 for further details.

The final dividend for the year ended 31 December 2017 was either paid in cash or issued as a scrip dividend equivalent of 27.2¢ per share. The final dividend for the year ended 31 December 2017 was paid in cash of $71,524,000 and 263,368 shares for the scrip dividend.

The interim dividends for 2018 and 2017 were either paid in cash or issued as a scrip dividend at the option of the shareholder. The interim dividend for the year ended 31 December 2018 was paid in cash of $35,694,000 (2017: $33,255,000) and 107,896 shares for the scrip dividend (2017: 108,769).

From the 2018 interim dividend, dividends have been and will continue to be declared in US Dollars, aligning shareholder returns with the primary currency in which the Group generates cash flow.

The Board has declared a final dividend of 28.6¢ per share to be paid on 12 June 2019 to shareholders registered on 10 May 2019, taking the total ordinary dividend per share for the year to 41.85¢ (2017: 39.8¢). The dividends will be paid in Sterling unless shareholders elect to be paid in US Dollars. The foreign exchange rates at which future dividends declared in US Dollars will be calculated is based on the average exchange rate in the five business days prior to the scrip dividend price being determined. On this occasion, the period will be between 22 May 2019 to 26 May 2019 inclusive.

A scrip dividend alternative will be offered to the owners of the Company.

When determining the level of dividend each year, the Board considers the ability of the Group to generate cash; the availability of that cash in the Group, while considering constraints such as regulatory capital requirements and the level required to invest in the business. This is a progressive policy and is expected to be maintained for the foreseeable future.

30 Contingencies and guarantees

The Group's subsidiaries are, like most other insurers, continuously involved in legal proceedings, claims and litigation in the normal course of business.

The following guarantees have also been issued:

(a) Hiscox Dedicated Corporate Member Limited (HDCM) and Hiscox Capital Ltd (HCL) provide assets under a Security and Trust Deed charged to Lloyd's of London, to meet any liabilities they occur from their interest in Syndicates 33 and 3624. At 31 December 2018, HDCM held £261 million of investments, £18 million of cash and a £20 million Letter of Credit in favour of Lloyd's of London under this arrangement. At 31 December 2018, HCL held £449 million of investments (2017: £485 million), £11 million of cash and a £20 million Letter of Credit in favour of Lloyd's of London under this arrangement.

(b) Hiscox plc continued with its Letter of Credit and revolving credit facility with Lloyds Banking Group, as agent for a syndicate of banks, at $800 million (2017: $500 million) which may be drawn in cash (under a revolving credit facility), Letter of Credit or a combination thereof. The terms also provide that upon request the facility may be drawn in a currency other than US Dollar. At 31 December 2018 $50.0 million (2017: $10.0 million) was utilised by way of Letter of Credit to support the Funds at Lloyd's requirement and no cash drawings were outstanding (2017: $nil).

(c) Hiscox Insurance Company Limited has arranged a Letter of Credit of £50,000 (2017: £50,000) with NatWest Bank plc to support its consortium activities with Lloyd's; the arrangement is collateralised with cash of £50,000 (2017: £50,000).

(d) The Council of Lloyd's has the discretion to call a contribution of up to 3% of capacity if required from the managed Syndicates.

(e) As Hiscox Insurance Company (Bermuda) Limited (Hiscox Bermuda) is not an admitted insurer or reinsurer in the USA, the terms of certain US insurance and reinsurance contracts require Hiscox Bermuda to provide Letters of Credit or other terms of collateral to clients. Hiscox Bermuda has in place a Letter of Credit Reimbursement and Pledge Agreement with Citibank for the provision of a Letter of Credit facility in favour of USA ceding companies and other jurisdictions, and also Letter of Credit facility agreements with National Australia Bank and Commerzbank AG. The agreements combined are a three-year secured facility that allowed Hiscox Bermuda to request the issuance of up to $600 million in Letters of Credit (2017: $400 million). Letters of Credit issued under these facilities are collateralised by cash, US government and corporate securities of Hiscox Bermuda. Letters of Credit under these facilities totalling $130.0 million were issued with an effective date of 31 December 2018 (2017: $100.7 million on a $400 million facility) and these were collateralised by USA government and corporate securities with a fair value of $152.8 million (2017: $115.8 million). In addition, Hiscox Bermuda maintained assets in trust accounts to collateralise obligations under various reinsurance agreements. At 31 December 2018 total cash and marketable securities with a carrying value of approximately $10.7 million (2017: $10.8 million) was held in external trusts. Cash and marketable securities with an approximate market value of $611.6 million (2017: $659.5 million) were held in trust in respect of internal quota share arrangements. Additionally, in 2018, $24.8 million was maintained in a trust account for credit enhancement purposes.

(f) Hiscox Europe Underwriting Limited has arranged bank guarantees with respect to their various office deposits for a total of €207,000 (2017: €207,000). These guarantees are held with ING Bank (Belgium) for €14,000 (2017: €14,000), ABN Amro (Netherlands) for €33,000 (2017: €33,000) and HypoVereinsbank-UniCredit (Germany) for €160,000 (2017: €160,000).

(g) Hiscox SA has arranged a bank guarantee with respect to the office in Luxembourg with a value of €42,000 (2017: €42,000). This guarantee is held with ING Bank (Luxembourg).

(h) See note 25 for a tax-related contingent liability.

31 Capital and lease commitments

Capital commitments

The Group's capital expenditure contracted for at the balance sheet date but not yet incurred for property, plant, equipment and software development was $1,391,000 (2017: $1,620,000).

Operating lease commitments

The Group acts as both lessee and lessor in relation to various offices in the UK and overseas which are held under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights. The Group also has payment obligations in respect of operating leases for certain items of office equipment. Operating lease rental expenses for the year totalled $15,303,000 (2017: $14,503,000). Operating lease rental income for the year totalled $530,000 (2017: $733,000).

The aggregate minimum lease payments required by the Group under non-cancellable operating leases, over the expected lease terms, are as follows:

		2018 $000	2017 (restated)* $000
No later than one year	Land and buildings	16,512	13,054
	Office equipment and other	712	777
Later than one year and no later than five years	Land and buildings*	48,875	44,645
	Office equipment and other	999	617
Later than five years	Land and buildings*	11,454	11,816
		78,552	70,909

*Minimum lease payments do not include leases that have not yet commenced, specifically the lease on 22 Bishopsgate that is expected to commence in 2021.

The total future aggregate minimum lease rentals receivable by the Group as lessor under non-cancellable operating property leases are as follows:

	2018 $000	2017 (restated)* $000
No later than one year	675	464
Later than one year and no later than five years	1,126	–
	1,801	464

*See note 2.1 for further details.

32 Principal subsidiary companies of Hiscox Ltd at 31 December 2018

Company	Nature of business	Country
Hiscox plc*	Holding company	Great Britain
Hiscox Insurance Company Limited	General insurance	Great Britain
Hiscox Insurance Company (Guernsey) Limited*	General insurance	Guernsey
Hiscox Holdings Inc.	Insurance holding company	USA (Delaware)
ALTOHA, Inc.	Holding company	USA (Delaware)
Hiscox Insurance Company Inc.	General insurance	USA (Illinois)
Hiscox Inc.	Underwriting agent	USA (Delaware)
Hiscox Insurance Company (Bermuda) Limited*	General insurance and reinsurance	Bermuda
Hiscox Dedicated Corporate Member Limited	Lloyd's corporate Name	Great Britain
Hiscox Holdings Limited**	Insurance holding company	Great Britain
Hiscox Syndicates Limited	Lloyd's managing agent	Great Britain
Hiscox ASM Ltd.	Insurance intermediary	Great Britain
Hiscox Underwriting Group Services Limited	Service company	Great Britain
Hiscox Capital Ltd*	Reinsurance	Bermuda
Hiscox Underwriting Ltd	Underwriting agent	Great Britain
Hiscox Europe Underwriting Limited	Insurance intermediary	Great Britain
Hiscox Société Anonyme*	General insurance	Luxembourg
Hiscox Assure SAS	Insurance intermediary	France
Direct Asia Insurance (Holdings) Pte Ltd	Holding company	Singapore
Direct Asia Insurance (Singapore) Pte Limited	General insurance	Singapore

*Held directly.
**Hiscox Holdings Limited held 38,030 shares in Hiscox Ltd at 31 December 2018 (2017: 38,030).

All principal subsidiaries are wholly owned. The proportion of voting rights of subsidiaries held is the same as the proportion of equity shares held.

33 Related-party transactions

Details of the remuneration of the Group's key personnel, presented in Sterling, are shown in the annual report on remuneration 2018 on pages 72 to 83. A number of the Group's key personnel hold insurance contracts with the Group, all of which are on normal commercial terms and are not material in nature.

The following transactions were conducted with related parties during the year.

(a) Syndicate 33 at Lloyd's

Related-party balances between Group companies and Syndicate 33 reflect the 27.4% interest (2017: 27.4%) that the Group does not own, and are as follows.

	Transactions in the income statement for the year ended		Balances outstanding (payable) at	
	31 December 2018 $000	31 December 2017 (restated)* $000	**31 December 2018 $000**	31 December 2017 (restated)* $000
Hiscox Syndicates Limited	**9,583**	11,921	**6,389**	16,342
Hiscox Group insurance carriers	**(14,337)**	(24,797)	**(67,404)**	(40,864)
Hiscox Group insurance intermediaries	**3,515**	2,806	**(6,856)**	(9,389)
Other Hiscox Group companies	**–**	–	**10,520**	1,125
	(1,239)	(10,070)	**(57,351)**	(32,786)

*See note 2.1 for further details. In addition, the 2017 comparatives have been restated to reflect the 27.4% interest that the Group does not own, previously disclosed as the 72.6% the Group does own. There is no impact on the reported Group's balance sheet, income statement and cash flow statement.

(b) Transactions with associates

Certain companies within the Group conduct insurance and other business with associates. These transactions arise in the normal course of obtaining insurance business through brokerages, and are based on arm's length arrangements.

	2018 $000	2017 (restated)* $000
Gross premium income achieved through associates	**1,453**	83,773
Commission expense charged by associates	**5,073**	22,806
Amounts payable to associates at 31 December	**–**	–
Amounts receivable through associates at 31 December	**41,119**	44,434

*See note 2.1 for further details.

Details of the Group's associates are given in note 14.

(c) Internal reinsurance arrangements

During the current and prior year, there were a number of reinsurance arrangements entered into in the normal course of trade between various Group companies. The related results of these transactions have been eliminated on consolidation.

34 Post balance sheet event

In response to the UK's decision to leave the European Union, the Group made some necessary changes to its business. These will ensure continuity of cover and settlement of existing claims to all its customers with European risks, so that it can continue to service its policyholders and claimants across Europe post-Brexit. To make these changes the Group used a legal insurance business transfer process known as a Part VII transfer to novate insurance contracts covering EU risks and written by Hiscox Insurance Company Limited (HIC) prior to Brexit to Hiscox SA (HSA), the Group's EU carrier based in Luxembourg.

The Part VII process is governed by the Part VII of the Financial Services and Markets Act 2000 and is subject to the approval of the High Court of England and Wales and the Royal Court of Jersey. These approvals have been received and became effective on 1 January 2019, which means the Part VII transfer has taken place and HSA is operational.

Following this transfer, Hiscox Europe Underwriting Limited (HEUL) was merged under a EU Cross Border Merger (CBM) into HSA combining the Group's European insurance intermediary and risk carrier operation on 1 January 2019.

These intra-group transactions will not have an impact on the Group's consolidated financial statements, except for a potential tax charge due to the Part VII transfer. The potential tax charge of this Part VII transfer has yet to be fully assessed by the Group and will be fully disclosed in 2019. In respect to the CBM transaction, the professional tax advice obtained indicates that the transaction should take place on a tax neutral basis. However, the Group is seeking tax clearances in certain territories to confirm the tax neutrality. As at the date of these accounts, the Group does not believe any tax charge will arise on the CBM.

Five-year summary

	2018 $000	2017 (restated)* $000	2016 (restated)* $000	2015 (restated)* $000	2014 (restated)* $000
Results					
Gross premiums written	**3,778,341**	3,286,021	3,257,897	2,972,712	2,894,316
Net premiums written	**2,581,486**	2,402,999	2,424,450	2,403,349	2,213,940
Net premiums earned	**2,573,639**	2,416,208	2,271,316	2,194,139	2,169,195
Profit before tax	**137,375**	39,692	480,773	330,417	380,812
Profit for the year after tax	**127,999**	33,904	456,967	320,929	356,218
Assets employed					
Intangible assets	**204,600**	186,038	153,418	185,546	165,276
Financial assets carried at fair value	**5,029,681**	5,139,643	4,702,121	4,294,730	4,413,001
Cash and cash equivalents	**1,288,851**	867,767	824,373	1,069,984	1,015,016
Insurance liabilities and reinsurance assets	**(4,244,900)**	(4,174,495)	(3,778,688)	(3,689,041)	(3,603,372)
Other net assets	**38,886**	349,428	353,596	386,160	278,641
Net assets	**2,317,118**	2,368,381	2,254,820	2,247,379	2,268,562
Net asset value per share (¢)	**819.1**	835.1	805.9	801.2	721.5
Key statistics					
Basic earnings per share (¢)	**45.1**	12.0	162.5	111.4	111.1
Basic earnings per share (p)	**33.9**	9.3	119.8	72.8	67.4
Diluted earnings per share (¢)	**44.3**	11.6	157.3	107.8	106.4
Diluted earnings per share (p)	**33.2**	9.0	116.0	70.5	64.5
Combined ratio (%)	**94.9**	99.9	84.2	85.0	83.9
Return on equity (%)	**5.6**	1.5	23.0	16.0	17.1
Dividends per share (¢)	**41.9**	39.8	35.0	36.1	36.2
Dividends per share (p)	**32.8**	29.0	27.5	24.0	22.5
Share price – high† (p)	**1,711.0**	1,470.0	1,097.0	1,059.0	735.0
Share price – low† (p)	**1,332.0**	997.5	900.5	707.5	624.5

*See note 2.1 for further details.
†Closing mid-market prices.

The five-year summary is unaudited.

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